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# A Shot Across the Bow: Changing the Paradigm of Foreign Direct Investment Review in the United States

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# A SHOT ACROSS THE BOW: CHANGING THE PARADIGM OF FOREIGN DIRECT INVESTMENT REVIEW IN THE UNITED STATES

## I. INTRODUCTION

What do voting machines and ports have in common? Surprisingly, both may implicate vital national security considerations.<sup>1</sup> In 2006, congressional concerns and public outcry precipitated investigations into the foreign ownership of ports and voting machines, a little anticipated consequence of increased concerns about national security following the events of September 11, 2001 that will test American commitment to its historic policy of open borders in foreign investment.<sup>2</sup>

In March 2006, the proposed acquisition of a British company, Peninsular & Oriental Steam Navigation Co. (P&O), by Dubai Ports World (DPW), a company owned by the government of Dubai in the United Arab Emirates (UAE), brought a little known inter-agency committee, the Committee on Foreign Investment in the United States (CFIUS), to the “intersection of the global economy and the war on terrorism.”<sup>3</sup> Under the direction of the Secretary of the Treasury, CFIUS reviews proposed foreign direct investment (FDI) within the framework of U.S. open investment policy, providing the President with a basis to restrict FDI where necessary to protect national security.<sup>4</sup> Following the World Trade

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1. See, e.g., Elisabeth Bumiller et al., *Threats and Responses: The Reaction; Panel Saw No Security Issue In Port Contract, Officials Say*, N.Y. TIMES, Feb. 23, 2006, at A1; Tim Golden, *U.S. Investigates Voting Machines' Venezuela Ties*, N.Y. TIMES, Oct. 29, 2006, at A11.

2. The acquisition of a British company involved in producing U.S. military aircraft and tanks by Dubai International Capital, a company based in the United Arab Emirates (UAE), failed to elicit similar concerns. Robert McMahon, *The Chill After the Ports Storm*, COUNCIL ON FOREIGN RELATIONS, May 23, 2006, [www.cfr.org/publication/10755/chill\\_after\\_the\\_ports\\_storm.html](http://www.cfr.org/publication/10755/chill_after_the_ports_storm.html).

3. Bill Spindle et al., *In Ports Furor, a Clash over Dubai*, WALL ST. J. Feb. 23, 2006, at A1. Shoe-bomber Richard Reid was a British citizen, yet no objections were raised that a British company operated U.S. ports. Eben Kaplan, *The UAE Purchase of American Port Facilities*, COUNCIL ON FOREIGN RELATIONS, Feb. 21, 2006, [www.cfr.org/publication9918/uae\\_purchase\\_of\\_american\\_port\\_facilities.htm](http://www.cfr.org/publication9918/uae_purchase_of_american_port_facilities.htm) [hereinafter Kaplan, *UAE Purchase*].

4. The President's authority to investigate the effects on national security of mergers, acquisitions, and takeovers is limited to those that “could result in foreign control of persons engaged in interstate commerce in the United States.” 50 U.S.C. app. § 2170. See, e.g., Bumiller et al., *supra* note 1.

Center attacks of September 11, 2001, investigations revealed the vulnerability of domestic infrastructure like airports, bridges, and ports to terrorist attack.<sup>5</sup> The acquisition of P&O would have given DPW, and through it, the government of Dubai, ownership of port leases at six major U.S. cities.<sup>6</sup> A media furor ensued, highlighting the concern that foreign ownership of domestic infrastructure itself represented a national security concern. Over twenty bills were introduced in Congress to address the threat to national security represented by direct foreign investment in the United States.<sup>7</sup> Two separate bills passed in the House and Senate respectively contain the framework for reform of the current regulatory regime, which centers power of review in CFIUS.<sup>8</sup>

CFIUS emerged more recently in the context of a controversy regarding foreign ownership of Smartmatic, a leading manufacturer of U.S. electronic voting machines. In this case, CFIUS reviewed the 2005 acquisition of Sequoia Voting Systems, a Californian company, by Smartmatic, a privately held Venezuelan company.<sup>9</sup> The swathe of business interests implicated in a foreign investment review process that sweeps both ports and voting machines into its purview elicits questions as to what we are trying to protect, and from whom.

This Note argues that the current regulatory scheme is preferable to the proposed legislative reform because the existing regime has been successful in maintaining the primacy of traditional U.S. open investment policy without compromising national security. The DPW and Smartmatic deals nonetheless reveal a central problem with the existing paradigm: the lack of public and congressional confidence that CFIUS has conducted an effective review. Three central issues emerge from this common problem. First, congressional oversight is required to ensure CFIUS abides by its implementing legislation. Second, enhanced congressional oversight may be necessary to protect transactions from un-

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5. See generally OFFICE OF HOMELAND SECURITY, NATIONAL STRATEGY FOR HOMELAND SECURITY (2002), [http://www.whitehouse.gov/homeland/book/nat\\_strat\\_hls.pdf](http://www.whitehouse.gov/homeland/book/nat_strat_hls.pdf) [hereinafter NATIONAL STRATEGY].

6. Audrey Hudson, *Foreign Ownership of U.S. Terminals Remains Unknown*, WASH. TIMES, Mar. 8, 2006, at A9.

7. ALAN P. LARSON & DAVID M. MARCHICK, FOREIGN INVESTMENT AND NATIONAL SECURITY, COUNCIL ON FOREIGN RELATIONS, COUNCIL SPECIAL REPORT No. 18, 25 (2006) [hereinafter LARSON & MARCHICK, FOREIGN INVESTMENT]; Greg Simmons, *Foreign Investment Still a Concern for Congress*, FOX NEWS, May 4, 2006, <http://www.foxnews.com/story/0,2933,194186,00.html>.

8. National Security Foreign Investment Reform and Strengthened Transparency Act, H.R. 5337, 109th Cong. (2006); Foreign Investment and National Security Act, S. 3549, 109th Cong. (2006).

9. Golden, *supra* note 1.

necessary political and public controversy. Third, although the CFIUS review process proceeds ad hoc, its reviews of specific transactions nonetheless reveal larger security vulnerabilities. Enhanced congressional oversight, properly delimited, could provide the opportunity to draft tailored legislation to meet the security risks thus exposed while allowing individual transactions to proceed. While the proposed legislative reform, to some extent, might accomplish these objectives, it does so at the risk of deterring foreign investment while rendering CFIUS less effective. Instead, to ensure that the United States continues to benefit from FDI, congressional oversight must be limited to the extent necessary to address these problems.

Prefatory to the analysis of the existing and proposed legislation, Part II of this Note reviews the interrelation between foreign investment policy and national security, and in Part III, the facts and circumstances of the DPW and Smartmatic transactions. Part IV articulates two different models for the regulation of FDI, using the existing and proposed legislation as examples. The analysis demonstrates that the existing paradigm provides a better result by favoring open investment over national security concerns and reveals, through application of the proposed paradigm to the facts of the DPW and Smartmatic transactions, that the proposed paradigm sacrifices open investment policy with little tangible security benefit. Part V identifies the key problems with the existing paradigm that emerge from this analysis, and proposes an alternative strategy more consistent with the traditional open investment policy of the United States while taking into account the evolving challenges of national security.

## II. COMPETING VALUES: OPEN INVESTMENT AND NATIONAL SECURITY

U.S. economic policy traditionally emphasizes the importance of open investment; in fact, much of the United States' current preeminence and past development may be attributed to its historically liberal policy regarding foreign investment.<sup>10</sup> Conventional wisdom maintains that increasing the interrelation of different economies unites disparate national interests and promotes stability.<sup>11</sup> At the same time, encouraging FDI in

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10. Gerald T. Nowak, Note, *Above All, Do No Harm: The Application of the Exon-Florio Amendment to Dual-Use Technologies*, 13 MICH. J. INT'L L. 1002, 1014 (1992) (noting that the Erie Canal and the Louisiana Purchase were both financed by foreign capital).

11. LARSON & MARCHICK, FOREIGN INVESTMENT, *supra* note 7, at 6; Eben Kaplan, *Foreign Ownership of U.S. Infrastructure*, COUNCIL ON FOREIGN RELATIONS, Feb. 13, 2007, [http://www.cfr.org/publication/10092/foreign\\_ownership\\_of\\_us\\_infrastructure.html](http://www.cfr.org/publication/10092/foreign_ownership_of_us_infrastructure.html) [hereinafter Kaplan, *Foreign Ownership*]; see also UNITED STATES GOVERNMENT

the United States creates reciprocal opportunities for U.S. companies abroad.<sup>12</sup> Foreign investment helps fuel robust growth in the U.S. economy by providing capital to finance demands for investment that exceed the domestic economy's supply.<sup>13</sup> Foreign companies in the United States produce a significant percentage of U.S. exports and jobs.<sup>14</sup> In addition, foreign dollars spent in the United States on research and development contribute to the modernization and development of valuable products and technology<sup>15</sup> or enable a particular company or corporate division to continue operating in the United States.<sup>16</sup>

Within this context, new national security concerns emerged following the September 11, 2001 attacks on the World Trade Center in New York. Citing the modern transformation of business and government operations and their shared interdependence on "critical physical and information

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ACCOUNTING OFFICE [GAO], FOREIGN INVESTMENT: CONCERNS IN THE BANKING, PETROLEUM, CHEMICALS, AND BIOTECHNOLOGY SECTORS, GAO/NSIAD-90-129, 4 (May 30, 1990) (arguing that "foreign investments . . . should encourage increased stability by linking the economic interests of . . . countries with those of the United States") [hereinafter GAO May 1990]; GAO, CONTROLLING FOREIGN INVESTMENT IN NATIONAL INTEREST SECTORS OF THE U.S. ECONOMY, GAO/ID-77-18, 38 (Oct. 7, 1977) [hereinafter GAO Oct. 1977]; Davis B. Bobrow & Robert T. Kudrle, *Economic Interdependence and Security: U.S. Trade and Investment Policy for a New Era*, 3 MINN. J. GLOBAL TRADE 61, 77 (1994) (pointing out that foreign investment is more important for high technology sectors of the U.S. economy than other parts).

12. Kaplan, *Foreign Ownership*, *supra* note 11; see also Bobrow & Kudrle, *supra* note 11, at 77.

13. JAMES K. JACKSON, FINANCING THE U.S. TRADE DEFICIT, CONGRESSIONAL RESEARCH SERVICE [CRS] RL33274, 11 (Feb. 14, 2006) ("foreign capital inflows are needed to fill the gap between the demand for capital in the economy and the domestic supply of capital"); CRAIG ELWELL, THE U.S. TRADE DEFICIT: CAUSES, CONSEQUENCES, AND CURES, CRS RL31032, 5 (Aug. 12, 2004).

It is an economic identity that the amount of investment undertaken by an economy will be equal to the amount of saving—that is, the portion of current income not used for consumption—that is available to finance investment. But for a nation, this identity can be satisfied through the use of both domestic and foreign saving, or, domestic and foreign investment.

*Id.*

14. The trade deficit was in excess of \$725 billion in 2005. Foreign companies provide 5.3 million American jobs (often with higher wages than U.S. jobs) and produce twenty-one percent of U.S. exports. Kaplan, *Foreign Ownership*, *supra* note 12. The U.S. trade deficit last year widened more than seventeen percent from the previous year, and the only way to finance this deficit is by attracting foreign investment. Bernard Wysocki, Jr. et al., *Port Debate Exposes Conflicts Between Security Needs and Foreign Investment*, WALL ST. J., Feb. 23, 2006, at A1.

15. See LARSON & MARCHICK, FOREIGN INVESTMENT, *supra* note 7, at 7.

16. See *id.* at 22.

infrastructures,” Congress enacted the Critical Infrastructures Protection Act of 2001.<sup>17</sup> Critical infrastructure “means systems and assets, whether physical or virtual, so vital to the United States that the incapacity or destruction of such systems and assets would have a debilitating impact on security, national economic security, national public health or safety, or any combination of those matters.”<sup>18</sup> This definition is the linchpin for subsequent homeland security and national defense legislation.<sup>19</sup> In the *National Strategy for Homeland Security*, the White House emphasized two axes of security vulnerability: infrastructure that delivers critical functions or services and the complex interdependency between them such that a successful attack at any point in these systems can reverberate throughout.<sup>20</sup> Threats include those presented by the privileged access of employees to information on “vulnerabilities, operations, and protective measures” for critical infrastructure or direct facilitation of attacks through provision of access to sensitive areas like loading docks, control centers, and airport tarmacs.<sup>21</sup>

Following the DPW deal, these broad national security concerns precipitated a reexamination of the nature and role of FDI in the United States.<sup>22</sup> Although Congress empowered the executive branch with broad authority in situations of national emergency,<sup>23</sup> the emergency powers do not apply extraterritorially.<sup>24</sup> Furthermore, foreign firms within the United States and abroad may be subject to influence by their home country governments or may suffer security breaches compromising sen-

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17. 42 U.S.C. § 5195c(a) & (b).

18. 42 U.S.C. § 5195c(e).

19. See generally NATIONAL STRATEGY, *supra* note 5. The *National Strategy for Homeland Security* identifies agriculture, food, water, public health, emergency services, government, defense industrial base, information and telecommunications, energy, transportation, banking and finance, chemical industry, postal, and shipping sectors as critical infrastructure. *Id.* at 29–30.

20. See *id.* at 30.

21. *Id.* at 34.

22. This Note uses the definition of foreign direct investment (FDI) provided in 15 C.F.R. § 806.15(a)(1), which states that FDI is “the ownership or control, directly or indirectly, by one foreign person of ten per centum or more of the voting securities of an incorporated U.S. business enterprise or an equivalent interest in an unincorporated U.S. business enterprise . . . .” 15 C.F.R. § 806.15(a)(1).

23. See, e.g., Trading with the Enemy Act, 50 U.S.C. app. § 5 (1917); International Emergency Economy Powers Act, 50 U.S.C. §§ 1701–1706 (1976); see Bobrow & Kudrle, *supra* note 11, at 80 (commenting that “the U.S. government has legal means to assure supply even from a foreign monopolist when its operations are located in the United States . . . the special emergency measures do not apply when the source of investment is located outside U.S. jurisdiction”).

24. Bobrow & Kudrle, *supra* 11, at 80.

sitive U.S. information.<sup>25</sup> The view that these risks warrant regulation of FDI in the United States reflects an underlying assumption that foreign companies, unlike U.S. companies, operate under competing interests that may undermine their compliance with U.S. laws and security.<sup>26</sup> With respect to the DPW transaction in particular, this view took concrete form when critics of the deal articulated concerns that Dubai's ports were a conduit for black market nuclear technology, that terrorists used Dubai's financial centers to circumvent U.S. economic sanctions and funnel funds, and that some September 11 terrorists were UAE citizens.<sup>27</sup>

The interrelationship between FDI and national security presents a dilemma: allow foreign ownership and tolerate an unquantifiable risk to national security or restrict foreign ownership and tolerate reduced capital and attendant business difficulties for U.S. firms.<sup>28</sup> Balanced against favoring the national security concern in this relationship is that the United States plays a significant role in defining global economic policy.<sup>29</sup> Tightening the reins on foreign investment in the United States may well reinforce isolationist urges elsewhere, with long-term consequences to American interests at home and abroad.<sup>30</sup> Given the interconnectedness of critical infrastructure,<sup>31</sup> greater security may require attracting foreign firms, not only because they provide expertise and capital, but because U.S. security depends on reciprocal security arrangements with both private and government owned and operated infrastructure worldwide.<sup>32</sup>

Striking the right balance between the competing values of open investment and national security remains especially important because examination of the data on foreign investment suggests that the United States has not used FDI as a vehicle for aligning foreign interests with its

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25. *Id.*; LARSON & MARCHICK, FOREIGN INVESTMENT, *supra* note 7, at 9–10.

26. Kaplan, *Foreign Ownership*, *supra* note 12; LARSON & MARCHICK, FOREIGN INVESTMENT, *supra* note 7, at 9.

27. Spindle et al., *supra* note 3; Bill Spindle & Yasmine El-Rashidi, *In Quest to Build A Financial Center, Hurdles for Dubai*, WALL ST. J., Mar. 2, 2006, at A1; Lawrence Lindsey, *Not For Sale to Foreigners*, WALL ST. J., Mar. 10, 2006, at A18.

28. See GAO, FOREIGN INVESTMENT: ANALYZING NATIONAL SECURITY CONCERNS, GAO/NSIAD-90-94, 26 (Mar. 1990) [hereinafter GAO Mar. 1990].

29. LARSON & MARCHICK, FOREIGN INVESTMENT, *supra* note 7, at 6.

30. See, e.g., *id.*; McMahon, *supra* note 2; Douglas Holtz-Eakin, Op-Ed., *You Can't Be CFIUS*, WALL ST. J., July 13, 2006, at A8.

31. Electricity, petroleum pipelines, trade, and the global transportation system are examples. See NATIONAL STRATEGY, *supra* note 5, at 35.

32. Ports and airports are examples of critical infrastructure that present a curious mixture of state and private interests both in the United States and worldwide. LARSON & MARCHICK, FOREIGN INVESTMENT, *supra* note 7, at 31.

own with equal consistency or success in all countries.<sup>33</sup> Although ninety percent of foreign investment in the United States derives from members of Organisation for Economic Co-operation and Development (OECD),<sup>34</sup> the vast majority of that investment originates in countries that are already U.S. allies.<sup>35</sup> In contrast, investments originating in the Middle East represent a small percentage of FDI in the U.S. economy, even though Middle Eastern countries are a significant destination of American goods and American FDI.<sup>36</sup> In 2004, Middle Eastern countries invested a relatively small \$192 million in hard U.S. assets, but Middle East oil exporters also held \$121.1 billion in U.S. securities, providing an untapped resource for investment in hard U.S. assets.<sup>37</sup> Similarly, Venezuela is a relatively insignificant percentage of FDI in the U.S. economy,<sup>38</sup> although American investment represents fifty-three percent of FDI in Venezuela.<sup>39</sup> The investments, valued at approximately \$10.8 billion, are diversified among petroleum, telecommunications, manufacturing, and finance sectors. The United States relies heavily on Venezuela

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33. See *supra* note 11 and accompanying text.

34. The OECD is the successor to the organization created to administer aid under the Marshall Plan following World War II. Today the organization is dedicated to the maintenance and development of free market economies. There are currently thirty member states, including the United States. See ORGANISATION FOR ECONOMIC CO-OPERATION AND DEVELOPMENT, ABOUT OECD, [http://www.oecd.org/about/0,2337,en\\_2649\\_201185\\_1\\_1\\_1\\_1\\_1,00.html](http://www.oecd.org/about/0,2337,en_2649_201185_1_1_1_1_1,00.html) (last visited May 27, 2007). The majority of foreign investment is in liquid assets; in 2004, "foreigners held \$1.9 trillion in U.S. corporate stocks, \$2.2 trillion in government securities, \$2.1 trillion in private bonds and \$2.9 trillion in debt . . . according to the Commerce Department's Bureau of Economic Analysis . . . \$2.7 trillion . . . is invested in hard assets." Wysocki, Jr. et al., *supra* note 14. Insofar as there are risks associated with liquid holdings in the United States that stem from the destabilizing effects of sudden withdrawals, increasing physical holdings of foreign firms provides ballast in the form of "a more permanent stake in the health of the U.S. economy." LARSON & MARCHICK, FOREIGN INVESTMENT, *supra* note 7, at 23.

35. The greater percentage of foreign investment in the United States comes from the United Kingdom and the European Union. See UNCTAD, WORLD INVESTMENT REPORT 2005 and UNCTAD WORLD INVESTMENT REPORT 2006 available at [www.unctad.org/fdistatistics](http://www.unctad.org/fdistatistics); see also U.S. DEPARTMENT OF STATE, BACKGROUND NOTE: UNITED KINGDOM, <http://www.state.gov/r/pa/ei/bgn/3846.htm> (last visited May 27, 2007).

36. MARY JANE BOLLE, MIDDLE EAST FREE TRADE AREA: PROGRESS REPORT, CRS RL32638, 5-7 (2006).

37. These numbers exclude Israel. Wysocki, Jr. et al., *supra* note 14.

38. Venezuelan FDI totals \$5.5 billion, compared with \$252 billion from the United Kingdom. U.S. DEPARTMENT OF STATE, FOREIGN DIRECT INVESTMENT IN THE UNITED STATES, <http://www.state.gov/r/pa/prs/ps/2006/63553.htm> (last visited May 27, 2007).

39. U.S. DEPARTMENT OF STATE, VENEZUELA 2005 INVESTMENT CLIMATE STATEMENT, [www.state.gov/e/eb/ifa/2005/43503.html](http://www.state.gov/e/eb/ifa/2005/43503.html) (last visited May 27, 2007), U.S. DEPARTMENT OF STATE, BACKGROUND NOTE: VENEZUELA, <http://www.state.gov/r/pa/ei/bgn/35766.htm> (last visited May 27, 2007).



for its oil needs, and the United States trade deficit is on the rise, weighing in at \$19.5 billion in 2004.<sup>40</sup> This data, which shows a vast untapped pool of foreign capital, suggests that by shifting the balance in favor of national security so as to preclude investment from countries like the UAE or Venezuela, the United States would lose a significant opportunity to increase economic interdependence, align foreign interests with its own, and thereby improve national security.

The controversy that emerged regarding the DPW and Smartmatic deals are manifestations of the tension between traditional open investment policy and increased national security concerns.<sup>41</sup> Insofar as FDI increases stability, and hence, security, by aligning national interests, the chilly reception of DPW, the retroactive scrutiny of the Smartmatic deal, and the proposed legislative reform fires a clear shot across the bow to foreign investors and may well discourage future investments.<sup>42</sup>

### III. THE DILEMMA IN ACTION: DUBAI PORTS WORLD AND SMARTMATIC TRANSACTIONS

#### *A. Dubai Ports World*

DPW is part of Ports Customs & Freezone Corp., a company owned by the government of Dubai.<sup>43</sup> The company first entered the world stage with the acquisition of the port facilities of CSX Corporation of Jacksonville, Florida, a U.S. company that had no ownership interests in U.S. ports, but the acquisition of which expanded DPW's existing reach in the Middle East and India to include ports in China.<sup>44</sup> DPW cited its expansion as commercially motivated as part of a larger trend to global con-

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40. U.S. DEPARTMENT OF STATE, BACKGROUND NOTE: VENEZUELA, <http://www.state.gov/r/pa/ei/bgn/35766.htm> (last visited May 27, 2007) (Venezuela is one of the United States' four major foreign sources of oil); U.S. DEPARTMENT OF STATE, VENEZUELA 2005 INVESTMENT CLIMATE STATEMENT, [www.state.gov/e/eb/ifa/2005/43503.html](http://www.state.gov/e/eb/ifa/2005/43503.html) (last visited May 27, 2007).

41. See discussion *infra* Part III.

42. See, e.g., LARSON & MARCHICK, FOREIGN INVESTMENT, *supra* note 7, at 6 (noting that "both . . . economic health . . . and . . . long term security depend on . . . a welcoming environment"); W. Robert Shearer, *The Exon-Florio Amendment: Protectionist Legislation Susceptible to Abuse*, 30 Hous. L. Rev. 1729, 1746-53 (1993) (discussing FDI and its role in building a robust economy, which itself provides national security, and advocating a total repeal of the review process to avoid discouraging FDI).

43. The government of Dubai is one of seven emirates that joined to form the UAE in 1971. See U.S. DEPARTMENT OF STATE, BACKGROUND NOTE: UNITED ARAB EMIRATES, <http://www.state.gov/r/pa/ei/bgn/5444.htm> (last visited May 27, 2007); Spindle et al., *supra* note 3.

44. Spindle et al., *supra* note 3.

solidation in the shipping and ports business.<sup>45</sup> The primary focus of DPW's attempt to acquire the British company, P&O, was to expand operations in China and India, thus complementing the geographic distribution of existing operations.<sup>46</sup> Although a company spokesperson stated that "[t]he U.S. is not the focus of the acquisition,"<sup>47</sup> the acquisition of P&O would give DPW control over terminals in six U.S. ports previously operated by the British company.<sup>48</sup>

The seventh largest port operator in the world, DPW operates in fourteen countries, provides support to U.S. military in Germany, Djibouti, and Dubai, and has been recognized for its high standards of port operation.<sup>49</sup> The senior management is composed of three citizens of the United States, one of Great Britain, two of India, one of the Netherlands, and four of Dubai. Of the four citizens of Dubai, two were educated at American universities.<sup>50</sup> The acquisition of P&O Ports North America, the U.S. operations of P&O, represented merely six to ten percent of the overall transaction; three of the leases to be acquired were joint ventures with U.S. companies.<sup>51</sup>

Critics of the deal issued statements in the press, precipitating a media uproar. Typically, reports focused on internal threats presented by the deal, citing UAE ties to terrorism, such that a UAE company operating U.S. ports would provide a conduit for terrorists to transport operatives and weapons to the United States.<sup>52</sup> While media reports and congres-

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45. *Testimony Before the Senate Commerce Committee*, 109th Cong. 2 (2006) (Statement of H. Edward Bilkey, Chief Operating Officer, Dubai Ports World), <http://commerce.senate.gov/pdf/bilkey-022806.pdf> [hereinafter Bilkey, *Testimony*].

46. Spindle et al., *supra* note 3.

47. *Id.* (quoting the Dubai Ports World spokesperson).

48. DPW's bid would affect operation of 850 port terminals in U.S. cities, including New York, New Jersey, Baltimore, New Orleans, Miami, and Philadelphia. *See* Hudson, *supra* note 6.

49. Bilkey, *Testimony*, *supra* note 45, at 1–2.

50. *Id.* at 2.

51. *Id.* at 2–3. The specific leases acquired are for port terminals located in Baltimore; Philadelphia, which was a fifty-fifty joint venture with Stevedoring Services of America; Miami, which was a fifty percent stake in Port of Miami Terminal Operating Company; New Orleans; and Newark, a fifty-fifty joint venture in the Port of Newark Container Terminal with Maersk Terminals. There were additional general stevedoring and cargo handling operations at additional locations and a passenger terminal in New York. *Id.* The \$6.8 billion deal involved ports in eighteen countries. *Q&A: U.S. Row Over Dubai Ports*, BBC NEWS, Mar. 9 2006, <http://news.bbc.co.uk/2/hi/business/4789368.stm> [hereinafter BBC NEWS, *Q&A*].

52. Critics specifically cited that two airplane hijackers involved in the 2001 World Trade Center attacks were from the UAE and that terrorist groups used the UAE a base of operations. Critics also emphasized that UAE is a primarily Arab and Muslim state. Kaplan, *UAE Purchase*, *supra* note 3; Gary Clyde Hufbauer, Op-Ed., *A Salute to Bush for*

sional statements inflamed public concerns, parties challenged the acquisition in courts in Great Britain, Florida, and New Jersey; all claims were rejected or rendered nugatory by subsequent developments.<sup>53</sup>

DPW contacted CFIUS to discuss the planned acquisition on October 17, 2005, and within two weeks, CFIUS engaged in an extensive preliminary review of the proposed transaction.<sup>54</sup> Official CFIUS review commenced on December 15, 2005.<sup>55</sup> Following its review, CFIUS recommended measures that would mitigate the national security concerns represented by the deal. Concessions included advance notice to the Department of Homeland Security (DHS) for changes in security arrangements, assignment of management of U.S. facilities to U.S. citizens, and the provision of confidential records relating to port management and employees without a subpoena.<sup>56</sup> DPW consented to the terms, and on January 17, 2006, CFIUS issued a formal letter allowing the acquisition

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*Standing Against Port Takeover Storm*, N.Y. DAILY NEWS, Feb. 27, 2006, available at <http://www.iie.com/publications/opeds/oped.cfm?ResearchID=602>.

53. A federal judge rejected New Jersey Governor Jon Corzine's request for an investigation and permission to inspect the documents submitted to CFIUS. Eller & Co, a stevedoring company in the Miami-Dade ports, attempted to block the takeover claiming that their business would be harmed by American retaliation if an Arab company were allowed to operate its ports. The Port Authority of New York and New Jersey filed suit in New Jersey state court to block the take over of operations at Port Newark. The plaintiffs sought relief on grounds that the landlord failed to seek approval of the tenants as required by the thirty year lease, emphasizing that as owners they needed to be "comfortable that whoever operates it is capable of it." They also alleged that the federal government had provided inadequate assurances about security issues. See *Ports Deal News Tracker*, WALL ST. J. ONLINE, Feb. 28, 2006, Mar. 1, 2006, & Mar. 2, 2006, <http://online.wsj.com/article/SB114071649414581503.html>.

54. Bilkey, *Testimony*, *supra* note 45, at 5.

55. *Id.* at 6. This sequence of events reflects standard operating practice for CFIUS. The governing statute imposes a short time-line for review, so a given transaction is extensively discussed before "official notice" is filed, triggering formal review and the statutory clock. See 31 C.F.R. § 800.401.

56. Specifically, DPW conceded it would: 1) maintain current levels of membership and cooperation in security arrangements; 2) provide DHS with thirty days advance notice of change in membership or cooperation in security arrangements; 3) operate U.S. facilities to the extent possible with current U.S. management; 4) designate a responsible corporate officer to serve as point of contact with the DHS on security matters; 5) provide relevant information promptly to DHS upon request; 6) assist and support law enforcement agencies (including disclosing information on the design, manufacture and operation of U.S. facilities); and 7) provide records relating to foreign operation direction, if any, of the U.S. facilities. Bilkey, *Testimony*, *supra* note 45, at 6-7; Robert Block, *Cherstoff Says U.S. Ports Takeover Would Tighten Grip on Security*, WALL ST. J., Mar. 27, 2006, at A3; Greg Hitt, *White House Cites Extra Safeguards in Ports Deal*, WALL ST. J., Feb. 23, 2006, at A3.

to proceed.<sup>57</sup> Following the media uproar, CFIUS, with the cooperation of DPW and P&O, commenced a second-stage extended investigation, which resulted in additional security concessions, including an interim agreement between DPW and P&O to permit the management and control of the North American operation to continue without direction or control from DPW until May 1, 2006 or until final approval of the transaction.<sup>58</sup> As furor over the deal refused to abate, DPW made additional unprecedented concessions: to install state-of-the-art radiation and gamma ray inspection devices at all current and future U.S. and foreign ports managed by DPW at company expense (estimated \$100 million cost); to grant the DHS a right to veto the choice of chief executive, board members, security officials, and all senior officers; and to create a supermajority of U.S. citizens on the board of directors.<sup>59</sup> DPW ultimately responded to American concerns by divesting its leases to American ports.<sup>60</sup>

#### B. Smartmatic

The transaction at issue in the Smartmatic controversy is its acquisition of Sequoia Voting Systems (SVS), completed in March 2005.<sup>61</sup> Unlike P&O, the target of the DPW acquisition, SVS is an American company based in California that has provided voting equipment nationwide since the 1890s.<sup>62</sup> Smartmatic is privately held, with ninety-seven percent owned by four Venezuelan founders.<sup>63</sup> It owes its recent rise to a series of voting contracts with the government of Venezuela, the first of which was awarded in 2004, the year Hugo Chávez was confirmed President of Venezuela by popular referendum.<sup>64</sup> The company, in conjunction with Bizta, another small start-up, won contracts from American competitors.<sup>65</sup> The proceeds from those contracts allowed Smartmatic to acquire

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57. Bilkey, *Testimony*, *supra* note 45, at 7.

58. *Id.* at 7–8.

59. DPW also volunteered to maintain all records relating to security operations on U.S. soil available on request and to establish a Security and Financial Oversight Board chaired by American citizens reporting annually to the DHS. Neil King, Jr., *DP World Tried to Soothe U.S. Waters*, WALL ST. J., Mar. 14, 2006, at A4.

60. BBC NEWS, *Q&A*, *supra* note 51.

61. Alphonso Chardy, *U.S. Digs for Vote-Machine Links to Hugo Chávez*, MIAMI HERALD, Oct. 28, 2006, at A1.

62. Press Release, Sequoia Voting Systems, Sequoia Voting Systems Responds to Venezuela-Related Rumors and Misinformation (May 11, 2006), <http://www.sequoia-vote.com/article.php?id=74>.

63. Chardy, *supra* note 61.

64. Golden, *supra* note 1.

65. *Id.*

SVS as part of a larger global sales and marketing plan to establish its leadership in electronic voting worldwide.<sup>66</sup> Following acquisition by Smartmatic, SVS's sales spiked, and its machines were used in sixteen states in 2006.<sup>67</sup>

Smartmatic, originally a single office headquartered in Florida, just prior to its acquisition of SVS, reincorporated in an elaborate structure of holding companies; critics pointed to this as evidence of the company's attempt to obfuscate its ownership.<sup>68</sup> In addition, Bizta, an entirely separate company, obtained a loan from the Venezuelan government, which received a twenty-eight percent stake in Bizta as guarantee and pursuant to which the Venezuelan government appointed a senior official to the company's board of directors.<sup>69</sup> According to critics, because two members of the Bizta board are also on the board of Smartmatic, the Venezuelan government could exert influence over Smartmatic,<sup>70</sup> even though the loan to Bizta was discharged in 2004 before Smartmatic bought Bizta in 2005.<sup>71</sup>

Thus, critics, citing concerns that the Venezuelan government may be able to wield influence over American elections by virtue of its connections to Smartmatic, brought the acquisition to the attention of President Bush in May 2006.<sup>72</sup> On October 29, 2006, Smartmatic and SVS issued a press release announcing they had voluntarily notified CFIUS, and had submitted information regarding ownership and security of their voting products for review.<sup>73</sup> In the same release, the company clarified that

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66. *Id.*

67. Bob Davis, *Smartmatic to Shed U.S. Unit, End Probe into Venezuelan Links*, WALL ST. J., Dec. 22, 2006, at A6 (also noting that the Justice Department had conducted an investigation into whether Smartmatic paid bribes to Venezuelan officials to win the 2004 election contract).

68. The holding companies were set up in trusts based in Delaware, the Netherlands, and the Caribbean. Golden, *supra* note 1.

69. Davis, *supra* note 67.

70. Golden, *supra* note 1.

71. Davis *supra* note 67.

72. See Golden, *supra* note 1.

73. Press Release, Sequoia Voting Systems, Smartmatic and Sequoia Voting Systems Announce Voluntary CFIUS Filing (Oct. 29, 2006), <http://www.sequoia.vote.com/article.php?id=79> (the press release identified three entrepreneurs as the primary owners: Antonio Mugica, with 78.8%; Alfredo Anzola, with 3.87%; and Roger Pinate, with 8.47%) [hereinafter SVS Oct. 29, 2006 Press Release]. In contrast, Representative Maloney asserted in a press release that:

[w]hen I first raised this case with Treasury, I thought that it was ripe for a CFIUS investigation, because the integrity of our voting machines is vital to national security. At that time, Smartmatic flatly refused to undergo a CFIUS

“[n]o foreign government or entity—including Venezuela—has ever held an ownership stake in Smartmatic.”<sup>74</sup> Subsequently, on December 22, 2006, Smartmatic obtained CFIUS approval to withdraw from the review process, and announced plans to sell SVS.<sup>75</sup> As with the DPW ports deal, the Sequoia voting machines became the subject of litigation when a suit was brought against New Jersey elections officials alleging that “the state did not properly certify the machines and that the equipment could not adequately protect against vote fraud.”<sup>76</sup>

While the DPW controversy should be viewed in light of domestic concerns regarding port security following the events of September 11, 2001, concerns regarding the Smartmatic transaction must be viewed in light of the vocal hostility of the Chávez government to the Bush administration, partisan voting controversies following *Bush v. Gore*,<sup>77</sup> and larger policy concerns regarding the security and integrity of electronic voting systems.<sup>78</sup>

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review. But . . . the company could not overcome the cloud of doubt . . . had they been able to, we would not be talking about a sale of Sequoia today.

Press Release, Rep. Carolyn Maloney (D-NY), Smartmatic Announces It Will Sell Sequoia Voting Systems, Withdraw from CFIUS Review (Dec. 22, 2006), [http://maloney.house.gov/index.php?option=com\\_content&task=view&id=1255&Itemid=61](http://maloney.house.gov/index.php?option=com_content&task=view&id=1255&Itemid=61) [hereinafter Maloney Press Release].

74. SVS Oct. 29, 2006 Press Release, *supra* note 73.

75. N.Y. TIMES, *Voting Machine Maker for Sale*, N.Y. TIMES, Dec. 23, 2006, at A17 (quoting Sequoia officials that the controversy would have no effect on the company’s role in U.S. elections); Press Release, Sequoia Voting Systems, Smartmatic Corporation and Sequoia Voting Systems Move to Align Corporate Structures with Future Business Goals (Dec. 22, 2006), <http://www.sequoiavote.com/article.php?id=82> (noting that the U.S. Election Assistance Commission had not raised any concerns regarding the use of the company’s products in the 2006 elections, that the products met the highest industry standards, and that the products had passed “extensive federal and state testing”).

76. Richard G. Jones, *Proof Sought on Reliability of Vote Units*, N.Y. TIMES, Feb. 17, 2007, at B4.

77. *Bush v. Gore*, 531 U.S. 98 (2000); Ian Urbina, *U.S. Panel is Said to Alter Finding on Voter Fraud*, N.Y. TIMES, Apr. 11, 2007, at A1.

78. The GAO issued a 2007 report documenting security problems in voting systems, the latest in a series of reports since 2001. GAO, ELECTIONS: ALL LEVELS OF GOVERNMENT ARE NEEDED TO ADDRESS ELECTRONIC VOTING SYSTEM CHALLENGES, GAO-07-576T (Statement of Randolph C. Hite, Mar. 7, 2007). Most recently, the stand-off between the United States and Venezuela was demonstrated when President Chávez called President Bush “the devil” at the United Nations and Venezuela’s challenge to the U.S. nomination of Guatemala to the United Nations Security Council. Warren Hoge, *Venezuelan’s Diatribe Seen as Fatal to U.N. Council Bid*, N.Y. TIMES, Oct. 25, 2006, at A6; *After 41 U.N. Ballots, Venezuela-Guatemala Logjam Persists*, N.Y. TIMES, Oct. 26, 2006, at A12; *see also* Michael Isikoff & Joseph Contreras, *Ortega and Ollie—Again*, NEWSWEEK, Nov. 6, 2006, at 9 (observing that the Bush administration is concerned

## IV. CHANGING THE PARADIGM

Following the Dubai Port World deal in 2006, two bills emerged as key contenders for CFIUS reform. Senator Richard Shelby of Alabama proposed the Foreign Investment and National Security Act of 2006 (S. 3549), which passed the Senate with unanimous consent.<sup>79</sup> A second bill, the National Security Foreign Investment Reform and Strengthened Transparency Act of 2006 (H.R. 5337), sponsored by Representative Roy Blunt of Missouri, passed the House with near unanimous approval.<sup>80</sup> Both seek to amend the Exon-Florio and CFIUS review process encapsulated in the Defense Production Act of 1950 and related executive orders. The way the current law and the proposed bill structure the CFIUS inquiry reflect two different views regarding the proper framework for analysis of risks presented by FDI. The paradigm reflected in the existing law may be characterized as a totality of the circumstances test, whereas the changes proposed in the Senate bill introduce a minimum threshold analysis. In the former, the significance of any one factor is weighed against the entire situation presented by the transaction. In the latter, certain types of activity and contacts trigger heightened scrutiny to determine if they are substantial enough to suggest impairment of national security. The differences between these two approaches reflect a fundamental shift in the relative primacy of open investment versus national security in the review process.

*A. The Current FDI Review Process: The Totality of the Circumstances Paradigm*

The principle inquiry in the existing Exon-Florio review process, which was first established in 1975<sup>81</sup> and expanded by Congress in 1988,<sup>82</sup> is triggered by voluntary notice from parties to a transaction.<sup>83</sup>

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Venezuelan President Chávez may be lending financial support to the re-election of ex-Sandinista leader Daniel Ortega in Nicaragua).

79. Foreign Investment and National Security Act, S. 3549, 109th Cong. (2006).

80. National Security Foreign Investment Reform and Strengthened Transparency Act, H.R. 5337, 109th Cong. (2006).

81. President Gerald Ford created CFIUS by executive order in 1975, but the executive branch had no authority to interfere in FDI aside from the President's powers to declare a national emergency or if regulatory authority under federal antitrust, environmental or securities laws. International Emergency Economic Powers, 50 U.S.C. §§ 1701–1706; Exec. Order No. 11,858, 40 F.R. 20,263 (May 7, 1975).

82. The review process in present form derives from a 1988 amendment to § 721 of the Defense Production Act (1950), the so-called Exon-Florio Amendment, which expanded presidential authority to block foreign acquisitions that threatened national security and formalized the CFIUS review process, which had proceeded on an informal basis pursuant to an executive order. The President delegated the authority granted him by the

Individual CFIUS members may also notify the committee of a transaction.<sup>84</sup> CFIUS, originally consisting of six members, has expanded to its present membership of twelve representatives of different departments and offices of the executive branch.<sup>85</sup>

In the two-prong inquiry, CFIUS must first determine whether there is credible evidence that a foreign person acquiring control may take action that threatens to impair national security and second, whether existing laws, other than Exon-Florio and the International Emergency Economic Powers Act, provide the President insufficient authority to protect national security in the matter before the President.<sup>86</sup> No particularized definition of “national security” was provided; legislators deliberately left the term to interpretation so as to ensure it would not be delimited by industry.<sup>87</sup>

Although notice is voluntary, consequences for failing to file are severe because failure to secure CFIUS approval or to fully disclose or to misrepresent in the process subjects the transaction to divestiture if at any

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1988 Exon-Florio Amendment to CFIUS via executive order. The Defense Production Act of 1950, 50 U.S.C. app. § 2170 (1994); Exec. Order No. 12,661, 40 F.R. 779 (Dec. 27, 1988); *see generally* JAMES K. JACKSON, THE EXON-FLORIO NATIONAL SECURITY TEST FOR FOREIGN INVESTMENT, CRS 22197, 2 (Feb. 23, 2006) (providing an overview of the legislative and regulatory history) [hereinafter JACKSON, NATIONAL SECURITY TEST].

83. 31 C.F.R. § 800.401(a) (voluntary notice by a party to a transaction). The Department of Treasury first promulgated guidelines in 1991. *See* JACKSON, NATIONAL SECURITY TEST, *supra* note 82, at 4.

84. 31 C.F.R. § 800.401(b).

85. Executive departments represented on CFIUS include: Department of Treasury (Chair), Department of Commerce, Department of State, Department of Homeland Security, Department of Justice, and the Department of Defense. Executive offices of the President represented on CFIUS include: Office of Management and Budget, Office of the U.S. Trade Representative, Council of Economic Advisers, Office of Science and Technology Policy, National Security Council, and the National Economic Council. *See* Saxton, *Committee Report*, *supra* note 86.

86. 50 U.S.C. app. § 2170(e); *see also* Jim Saxton, *Committee on Foreign Investment in the United States*, JOINT ECONOMIC COMMITTEE RESEARCH REPORT 109-34, Mar. 2006, available at [www.house.gov/jec](http://www.house.gov/jec) [hereinafter Saxton, *Committee Report*]. Industries such as power, banking, maritime, and aircraft are governed by industry-specific regulation that imposes limitations on foreign ownership. A report to Congress by the Comptroller General in 1977 examined the statutory framework governing these different sectors of “national interest” and concluded there was no need to introduce an additional layer of review on the influx of foreign capital because existing legislation already specifically addressed the risks of foreign ownership in those industries. GAO Oct. 1977, *supra* note 11, at 6–22, 38; *see also* JACKSON, NATIONAL SECURITY TEST, *supra* note 82, at 3.

87. “Critical technologies” are defined, but “national security” is not. *See* 50 U.S.C. app. § 2170 (k)(2); *see also* JACKSON, NATIONAL SECURITY TEST, *supra* note 82, at 3 (citing 134 CONG. REC. H2118 (daily ed. Apr. 20, 1988)).



time the acquisition raises security concerns.<sup>88</sup> Compliance gives the transaction the benefit of a safe harbor provision, minimizing risk of subsequent review or action by the President.<sup>89</sup>

The two-prong inquiry whereby CFIUS adduces the existence of credible evidence of a threat to national security and whether existing laws provide the President with sufficient authority to protect national security governs both phases of the CFIUS process: an initial thirty-day review and a second-stage forty-five day investigation.<sup>90</sup> If, upon completing the first-stage thirty day review, CFIUS is unable to resolve security concerns with the parties to the transaction, the companies will either withdraw notice to provide more time, or if withdrawal is not feasible either because the company refuses or the security risks are too great, CFIUS will proceed to a second stage, entailing a more extensive forty-five day investigation.<sup>91</sup> At all stages of the process, CFIUS proceeds by consensus; consequently, the objection of any one of the member agencies at the conclusion of the first-stage thirty day review triggers the second-stage forty-five day investigation, and upon conclusion of the investigation, if CFIUS cannot reach consensus regarding a recommended course

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88. 50 U.S.C. app. § 2170(d); 31 C.F.R. § 800.601(d)–(e).

89. 31 C.F.R. § 800.601(d). The regulation states that:

[a]ll authority available to the President under section 721(d), including divestment authority, shall remain available at the discretion of the President in respect of acquisitions which have been concluded at any time on or after the effective date, but only if the purpose for which divestment or other appropriate relief is sought is based on facts, conditions, or circumstances existing at the time the transaction was concluded. Such authority shall not be exercised if:

- (1) The Committee, through its Staff Chairman, has in writing advised a party (or the parties) that a particular transaction, with respect to which voluntary notice was attempted, was not subject to section 721;
- (2) The Committee has previously determined under § 800.502 not to undertake an investigation of the acquisition when proposed, pending, or completed; or
- (3) The President has previously determined not to exercise his authority under section 721 with respect to that acquisition.

*Id.*

90. 50 U.S.C. § 5170(e); 31 C.F.R. § 800.501(a); *see also* LARSON & MARCHICK, FOREIGN INVESTMENT, *supra* note 7, at 13.

91. A company may, provided CFIUS approves, withdraw its notice at any time prior to the president's final decision. 31 C.F.R. § 800.505; *see also* LARSON & MARCHICK, FOREIGN INVESTMENT, *supra* note 7, at 14–15. For review periods, *see* 31 C.F.R. § 800.404(a) (commencing thirty day review period) and § 800.504(a) (conclusion of investigation after forty-five days).

of action for the President, the report to the President must represent dissenting views.<sup>92</sup>

The existing law, whereby the mechanism is permissive, discretionary, ad hoc, and incorporates discreet reporting requirements, provides an example of a totality of the circumstances paradigm under which national security concerns are subordinated to the open investment principle. For example, although an investigation is required where the party acquiring control is a foreign government or person acting on behalf of a foreign government, the statute is otherwise permissive, accepting voluntary notifications from parties to a transaction.<sup>93</sup> Furthermore, Exon-Florio stipulates merely that CFIUS “may” consider several different factors in its inquiry, including the effect of the proposed investment on domestic production for projected national defense requirements, the consequences of sales of military technology to countries of concern with respect to terrorism and weapons of mass destruction, and the potential effects of the proposed transaction on U.S. defense technology leadership.<sup>94</sup> Consequently, the inquiry underlying the review and investigation entails consideration of both the past conduct and future intentions of the individual investor, and to a lesser extent, the nation of origin of the invest-

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92. 31 C.F.R. § 800.504; LARSON & MARCHICK, FOREIGN INVESTMENT, *supra* note 7, at 14.

93. On voluntary notice, see 31 C.F.R. § 800.601. The mandatory investigation requirement concerning foreign governments was introduced by the so-called Byrd Amendment to the Defense Production Act of 1950, enacted in the National Defense Authorization Act for Fiscal Year 1993, Pub. L. No. 102-484, § 837(b) (1992), and codified as 50 U.S.C. app. § 2170 (b). *See also* JACKSON, NATIONAL SECURITY TEST, *supra* note 82, at 3, note 11.

94. The statute specifically suggests consideration of:

1) domestic production needed for projected national defense requirements, 2) the capability and capacity of domestic industries to meet national defense requirements, including the availability of human resources, products, technology, materials, and other supplies and services, 3) the control of domestic industries and commercial activity by foreign citizens as it affects the capability and capacity of the United States to meet the requirements of national security, 4) the potential effects of the . . . transaction on the sales of military goods, equipment, or technology to any country (A) identified by the Secretary of State . . . or (B) listed under . . . the ‘Nuclear Non-Proliferation Special Country List’ . . . and 5) the potential effects of the . . . transaction on United States international technological leadership in areas affecting United States national security.

50 U.S.C. app. § 2170 (f); *see also* JACKSON, NATIONAL SECURITY TEST, *supra* note 82, at 3–4.

ment, but only insofar as this presents credible evidence of an impairment of national security.<sup>95</sup>

While the current law does not define national security, suggesting the scope of review is unlimited, in fact, the compass of these factors delineate the core inquiry for CFIUS, largely limiting its purview to acquisitions of controlling interests that have measurable consequences for the present and future capacity to meet defense production requirements.<sup>96</sup> At the same time, the undefined scope of national security encourages voluntary notification of CFIUS because where there is a question regarding whether or not a given transaction will implicate national security concerns, corporations seek to benefit from the safe harbor provision to minimize the risk of subsequent divestment.<sup>97</sup> Furthermore, in declining to specify national security or to articulate a mandatory list of factors for consideration, the current law permits CFIUS discretion to prioritize transactions for review and investigation, permitting it to traverse industries, formulations of management control, and chains of relationships to assess how, in the facts of a specific case, the transaction may implicate national security concerns.<sup>98</sup>

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95. On the balance between consideration of past and future conduct of an investor in evaluating security risks, see GAO May 1990, *supra* note 11, at 3; GAO Mar. 1990, *supra* note 28, at 12; GAO, NATIONAL SECURITY REVIEWS OF FOREIGN INVESTMENT, GAO/T-NSIAD-91-08, 9–10 (Feb. 26, 1991) (Testimony of Allan I. Mendelowitz) [hereinafter GAO Feb. 1991]. The Department of Treasury regulations define “control” as “the power, direct or indirect, whether or not exercised . . . to determine, direct, take reach or cause decisions regarding . . .” matters including: the transfer of principal assets; dissolution; closing or relocation of production, research, or development facilities; termination or non-fulfillment of contracts; and amendment of the entity’s operative agreement. The regulation also stipulates that where more than one foreign person has an interest, “consideration will be given to factors such as whether the foreign persons are related and/or whether they have commitments to act in concert.” 31 C.F.R. 800.204 (a) & (b).

96. “They required policy judgments about the consequences of dependence on foreign semiconductor firms for both the U.S. civilian and military sectors. Such decisions would require making assumptions about the Japanese firm’s intentions regarding the market power and technology transfer that it would gain from the acquisition.” GAO Mar. 1990, *supra* note 28, at 22 (discussing a Japanese firm’s proposed purchase of a U.S. semiconductor producer).

97. *Id.* at 14 (noting that failure to “provide a clear definition of national security or the criteria [meant] attorneys representing potential foreign investors feel compelled to clear most foreign investments with CFIUS before completing the transactions”); GAO DEFENSE TRADE: IDENTIFYING FOREIGN ACQUISITIONS AFFECTING NATIONAL SECURITY CAN BE IMPROVED, GAO/NSIAD-00-144, 5 (June 2000) [hereinafter GAO June 2000].

98. “CFIUS evaluates investment on a case-by-case basis and is able to gather extensive information about the firms involved . . . CFIUS does not perform analyses of foreign investment by industry sector, nor does it examine other larger questions which have arisen in public debate.” GAO Feb. 1991, *supra* note 95, at 9–10.

In addition, specific transactions are typically approved pending implementation of certain conditions, including limitations on involvement of an acquiring foreign party through, for example, addition of American citizens to the board.<sup>99</sup> These limitations are specifically tailored to address the security concerns of different agencies and are implemented in mitigation agreements. These agreements may include penalties for non-compliance and entail obligations greater than those usually required of domestic companies.<sup>100</sup> If no measures are perceived adequate to address the national security concerns raised by the transaction, CFIUS may recommend the President block the deal.<sup>101</sup>

Strict requirements for confidentiality govern the review and investigation process, and as a corollary, the reporting requirements to Congress are limited. The statute, in its current form, requires a report to the Secretary of the Senate and the Clerk of the House of Representatives only upon the President's final determination whether or not to take action.<sup>102</sup> The President's decision-making authority is only triggered upon completion of the discretionary second-stage forty-five day investigation by CFIUS.<sup>103</sup> The statute also requires a report to Congress every four years, which is intended to assist Congress in its oversight responsibilities by providing an assessment of whether the FDI activity in the prior four-year period provides credible evidence of a coordinated state-driven strategy to erode U.S. critical technology leadership.<sup>104</sup> The limited and

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99. For example, the acquisition of IBM's personal computer business by Chinese computer-maker Lenovo was approved provided it included additional security measures. See McMahon, *supra* note 2. Approval of the 2000 acquisition of Verio, Inc., an Internet service provider, by Nippon Telephone and Telegraph Company was contingent upon a strict prohibition against Japanese government involvement; the 2003 acquisition of Global Crossing, Ltd. by Hong Kong Hutchinson Whampoa Ltd. and Singapore Technologies Telemedia was contingent upon the passivity of Hutchison in management because of Hutchinson's connections to the Chinese military. Hutchinson eventually withdrew but Technologies Telemedia proceeded based on a concession to place Americans on the board of Global Crossing. JACKSON, NATIONAL SECURITY TEST, *supra* note 82, at 5.

100. LARSON & MARCHICK, FOREIGN INVESTMENT, *supra* note 7, at 11–12.

101. See 31 C.F.R. 800.504(b); LARSON & MARCHICK, FOREIGN INVESTMENT, *supra* note 7, at 11–12.

102. 50 U.S.C. app. § 2170 (g). Prior to the 1992 amendments, the President was only required to report to Congress if he exercised authority to block an acquisition. GAO, DEFENSE TRADE: MITIGATING NATIONAL SECURITY CONCERNS UNDER EXON-FLORIO COULD BE IMPROVED, GAO-02-736, 1 (Sept. 2002) [hereinafter GAO Sept. 2002].

103. 31 C.F.R. § 800.504.

104. For example, through acquisition of U.S. companies engaged in the research, development, and production of critical technologies or through industrial espionage. 50 U.S.C. app. § 2170 (k)(1).

discreet nature of these reporting requirements reflects an overall emphasis on discretion and confidentiality.

The totality of the circumstances paradigm reflected in the current law, characterized, as described above, by a voluntary, discretionary, and ad hoc review mechanism with limited reporting requirements, is responsive to the problem that threats to national security are likely to change over time and the nature of the threat presented by any given transaction is highly fact specific. The broad scope of "national security" preserves executive discretion to respond to these threats as they emerge.<sup>105</sup> Simultaneously, the scope of the factors the statute suggests for review allows for effective prioritization of resources in response to these emerging threats. In addition, the entirely voluntary notification system avoids the appearance of a mandatory screening process while ensuring adequate review of transactions that entail security concerns.<sup>106</sup> This is reinforced by a strong incentive to provide notice, because the transaction may be subject to divestment at any time.<sup>107</sup> The reliance on negotiated mitigation agreements ensures that the means are narrowly tailored to the specific potential negative security consequences of a transaction while minimizing the risk that a particular transaction could be burdened with the costs of larger national security concerns.<sup>108</sup> Finally, the strict confidentiality requirements and limited reporting means reviews are, for the most part, safely sequestered from the political arena.<sup>109</sup>

On the other hand, the existing regime may be criticized as under-inclusive. Reliance on a system of voluntary notification likely results in under-reporting of transactions that present security risks, as some would

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105. See, e.g., Alan F. Holmer, Judith H. Bello, & Jeremy O. Preiss, *The Final Exon-Florio Regulations on Foreign Direct Investment: The Final Word or Prelude to Tighter Controls?*, 23 LAW & POL'Y INT'L BUS. 593, 609 (1992).

106. *Id.* at 595, 609–610 (observing that the open definition of national security encourages filing, and that the burdens are small because parties are free to consult with CFIUS to elicit guidance, especially in the context of large corporate transactions); LARSON & MARCHICK, *FOREIGN INVESTMENT*, *supra* note 7, at 11 (discussing the "specter" of mandatory investment screening and noting that the current regime encourages filing if there is "any possibility that a transaction might raise national security issues").

107. 50 U.S.C. app. § 2170 (d); see also Saxton, *Committee Report*, *supra* note 86 (noting that "compliance is very high because the President may order the divestment of a domestic acquisition at any time in the future if the foreign acquirer did not notify CFIUS").

108. See, e.g., Matthew R. Byrne, Note, *Protecting National Security and Promoting Foreign Investment: Maintaining the Exon-Florio Balance*, 67 OHIO ST. L.J. 849, 890–91, 904 (2006) (discussing benefits of mitigation agreements).

109. S. REP. NO. 109-264, 12 (2006); see LARSON & MARCHICK, *FOREIGN INVESTMENT*, *supra* note 7, at 15–17 (discussing the generally limited involvement of both the legislative and executive branches, contributing to an apolitical review process).

argue was the case with Smartmatic.<sup>110</sup> Moreover, the discretionary review may fail to take into account the national security implications of a particular transaction in its broader geo-political context, as some would argue was the case with DPW.<sup>111</sup> Similarly, the high order assigned to confidentiality comes at the expense of congressional and public confidence in the adequacy of the review.<sup>112</sup> Finally, permissive withdrawal regulations may allow an end-run on the review process because CFIUS does not monitor drop-outs.<sup>113</sup> This problem is replicated in the failure to monitor and enforce compliance with formal mitigation agreements.<sup>114</sup> Both instances permit a risk that deals presenting security concerns remain unaddressed.<sup>115</sup>

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110. Maloney Press Release, *supra* note 73 (Rep. Maloney commenting on Smartmatic deal). The existing law does not always reach privately owned or smaller companies, which may exclude “some of the most advanced technologies being developed.” GAO Mar. 1990, *supra* note 28, at 15; *see also* GAO June 2000, *supra* note 97, at 7. This report identified three transactions that were notified to member agencies but had not been reported to CFIUS. These included a 1999 acquisition of a U.S. manufacturer of ceramic body armor by a German firm; a 1998 acquisition of a U.S. laser manufacturer by a French firm; and a 1995 acquisition of a U.S. bearing manufacturer by a Hong Kong firm. The ceramic body armor manufacturer and the bearing manufacturer could have been captured by CFIUS because the companies deal in classified products that required Department of Defense reporting; the laser manufacturer cancelled its defense contracts, and did not believe its business fell within the purview of Exon-Florio. In all three cases, the firms agreed to cooperate with CFIUS. *Id.* at 10–13.

111. As an example, critics of CFIUS handling of the DPW deal commented that the current review process does not consider the underlying conditions in the UAE and the company’s vulnerability to infiltration and corruption. Kaplan, *UAE Purchase*, *supra* note 3 (quoting Congressman Peter King (R-NY)). Critics also expressed concern that the scope of interests encompassed in national security review were limited to those parties about whom threatening intelligence was reported and where the acquisition would affect export-control technologies or classified contracts; it was not expanded to include consideration of U.S. critical infrastructure. Letter from Rep. Bennie Thompson to Comptroller General David Walker, (Feb. 23, 2006), <http://hsc.house.gov/about/subcommittees.asp?ID=47&SubSection=0&Issue=0&DocumentType=0&PublishDate=0&subcommittee=8>.

112. S. REP. NO. 109-264, *supra* note 109, at 2; JACKSON, NATIONAL SECURITY TEST, *supra* note 82, at 4.

113. The GAO reported that two deals were completed prior to filing with CFIUS where notification was withdrawn because suitable mitigation measures could not be agreed upon, and the companies failed to re-file. The GAO concluded “[a]s a result, potential threats to national security . . . remained.” GAO Sept. 2002, *supra* note 102 at 2.

114. *Id.*

115. *Id.* at 12 (discussing the need for post-mitigation agreement monitoring).

*B. The Senate Bill: The Minimum Threshold Paradigm*

Following the DPW imbroglio, the Senate sought to reform the review process.<sup>116</sup> In comparison to the existing totality of the circumstances regime, the Senate bill effects a paradigm shift by incorporating a type of minimum threshold analysis under which the review mechanism is mandatory, categorical, and incorporates expansive reporting requirements.<sup>117</sup> The proposed bill retains the mandatory investigation of investments by foreign governments or on behalf of a foreign government.<sup>118</sup> In addition, where the transaction implicates control of critical infrastructure or where the security risks identified through review of an expanded list of factors and, in both instances, the security concerns are unmitigated, the bill requires CFIUS to undertake a forty-five day investigation.<sup>119</sup> Like the existing law, the bill declines to define “national security,” and retains the core factors for consideration in review and investigation discussed above, but limits the discretion of CFIUS by making their consideration mandatory.<sup>120</sup> The bill also introduces new factors, including, *inter alia*, potential effects on critical infrastructure and technologies, whether the country of origin is a potential regional military threat, and individual country assessments.<sup>121</sup> The incorporation of

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116. This has been a persistent concern with respect to the Exon-Florio review process and it has elicited not infrequent GAO reports. *See* GAO, DEFENSE TRADE: NATIONAL SECURITY REVIEWS OF FOREIGN ACQUISITIONS OF U.S. COMPANIES COULD BE IMPROVED, GAO-07-661T, 8 (Mar. 23, 2007) (Statement of Ann M. Calvaresi-Barr) (discussing a series of GAO reports since 2000) [hereinafter GAO Mar. 2007].

117. S. 3549 § 2.

118. The bill changes the voluntary notice provisions with regard to any transaction involving a foreign government and critical infrastructure by making notification of CFIUS in both of those circumstances mandatory, with penalties for non-compliance to be promulgated by CFIUS following enactment of the bill. *Id.* § 2(b)(5).

119. *Id.* § 2 (b)(1)(A)(ii) & (b)(1)(B).

120. *Id.* § 2(g) (“For purposes of determining whether to take action . . . and for purposes of reviews and investigations . . . *shall* consider . . .”) (emphasis added). On the decision not to define “national security” for the purposes of CFIUS review, see *supra* notes 87 & 97.

121. S. 3549 § 2(g)(1), (g)(2), & (g)(6)(B). Altogether, § 2(g) requires consideration of:

- (1) potential effects on United States critical infrastructure, including major energy assets;
- (2) potential effects on United States critical technologies;
- (3) domestic production needed for projected national defense requirements;
- (4) the capability and capacity of domestic industries to meet national defense requirements, including the availability of human resources, products, technology, materials, and other supplies and services;
- (5) the control of domestic industries and commercial activity by foreign citizens as it affects the capability and capacity of the United States to meet the requirements of national security;

these particular factors and the fact that they are mandatory introduces greater structure into the CFIUS inquiry, and creates a priori assumptions about what kinds of conduct and activity give rise to a threat to impair national security, reflecting a departure from the principle that has governed CFIUS in the past: ownership itself is a small part of a given vulnerability.<sup>122</sup>

By incorporating critical infrastructure and technology as mandatory criteria, the bill would require CFIUS to review and investigate transactions with unmitigated security risks that occur in any of the twenty-two key critical infrastructure industries, implicating transactions in areas as diverse as food supply and highways, bridges, and vaccinations.<sup>123</sup> The same is true for critical technologies, which encompass dual-use technologies, and thus, technologies used for both private commercial and defense contracting purposes are brought squarely within the purview of CFIUS review.<sup>124</sup> The incorporation of these specific categories of indus-

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(6) the potential effects of the proposed or pending transaction on sales of military goods, equipment, or technology to any country (A) identified by the Secretary of State (i) . . . as a country that supports terrorism; (ii) . . . as a country of concern regarding missile proliferation; or (iii) . . . as a country of concern regarding the proliferation of chemical and biological weapons; (B) identified by the Secretary of Defense as posing a potential regional military threat to the interests of the United States; or (C) listed . . . on the 'Nuclear Non-Proliferation Special Country list' . . . ; (7) the potential effects of the proposed or pending transaction on United States international technological leadership in areas affecting United States national security; (8) the long term projection of United States requirements for sources of energy and other critical resources and materials; and (9) the assessments developed under subsection (c)(7) of the country in which the foreign persons acquiring United States entities are based.

*Id.* § 2(g).

122. Kaplan, *Foreign Ownership*, *supra* note 12 (quoting Douglas Holtz-Eakin and Todd Malan).

123. The law introduces a requirement that all transactions resulting in foreign control of "critical infrastructure" as defined in the Defense Production Act of 1950 and the Homeland Security Act of 2002, and is intended "to create a realistic standard by which CFIUS should measure the potential impact on national security," while allowing CFIUS to promulgate regulations that "exclude from mandatory investigation commercial assets that clearly do not by themselves constitute critical infrastructure." The provisions exclude cases that are resolved through prior mitigation agreements. S. REP. NO. 109-264, *supra* note 109, at 7; *see also* JOHN MOTEFF & PAUL PARFOMAK, CRITICAL INFRASTRUCTURE AND KEY ASSETS: DEFINITION AND IDENTIFICATION, CRS RL 32631 (Oct. 1, 2004) (discussing evolution of the concept of critical infrastructure).

124. *See generally* Nowak, *supra* note 10 (analyzing the potential application of the 1992 amendments to Exon-Florio to dual-use technologies for protectionist ends, which would result in the diversion of foreign investment from the United States to foreign competitors, ultimately weakening the defense industrial base).



tries as factors for consideration necessarily entails a shift from a primarily management control-based inquiry focused on issues of defense supply to a broader inquiry that creates a categorical presumption of risk based on foreign ownership of property, including purely physical security.<sup>125</sup>

Similar consequences follow from the introduction of mandatory consideration of individual country assessments. Under the bill, CFIUS must consider individual country assessments when evaluating the risk of the proposed transaction not only with respect to a foreign government, but also with respect to an investment contemplated by a private citizen of that nation.<sup>126</sup> Individual country assessments, to be issued following enactment of the bill, encompass: (i) a country's past adherence to non-proliferation control regimes; (ii) the country's past relationship with the United States, specifically the country's record on cooperation with the United States in counter-terrorism efforts; and (iii) the risk the country presents with respect to transshipment and diversion of technologies, especially those with military applications and entails analysis of the country's national export control laws and regulations.<sup>127</sup>

As with the incorporation of the critical infrastructure and technologies requirement, the country assessments dramatically expand the scope of the current review. The elements encompassed in the country assessment assign greater weight to historical factors in considering the risk of a potential investment than exist in the current paradigm.<sup>128</sup> Insofar as the country assessment must be applied to private individuals as well as governments or persons acting on behalf of governments, the assessment creates a categorical presumption of risk with respect to private invest-

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125. See LARSON & MARCHICK, *FOREIGN INVESTMENT*, *supra* note 7, at 29 (recommending Congress refrain from incorporating critical infrastructure into the review process, and noting that "[t]he administration and Congress should work together to determine how best to protect critical infrastructure, regardless of who owns a particular company"). CFIUS' operative definition of control is provided in the regulations promulgated under the existing law, and may or may not be retained if the bill is passed. The current operational definition of control resides in 31 C.F.R. § 800.204.

126. S. 3549 § 2(g).

127. *Id.* § 2(c)(7).

128. In the current law, where a totality of the circumstances review is conducted, the past conduct and future plans of the individual investor, and to a lesser extent, the investors country of origin, are considered but only insofar as they implicate national security in light of the risk presented by the overall transaction, and thus, no categorical presumption against certain countries is created. See *supra* notes 93–94 and accompanying text.

ment from those countries, based purely on the individual investor's citizenship.<sup>129</sup>

As with the existing statute, the proposed bill requires strict confidentiality, but enhances congressional oversight by introducing expansive reporting requirements.<sup>130</sup> These include notice to Congress upon initiation and completion of the first-stage thirty-day review, and if the second-stage investigation is deemed necessary or required by the statute (as with governments party to a transaction) upon initiation and conclusion of the forty-five day second-stage investigation.<sup>131</sup> Both concluding notices require certification by the Chair and Vice Chair of CFIUS and include a report as to measures taken, factors considered, and ultimate decisions.<sup>132</sup> CFIUS must provide these notices to the Majority and Minority Leaders of the Senate, the ranking members of the Committee on Banking, Housing and Urban Affairs and of any committees in the House and Senate with oversight of an agency on CFIUS that is assigned to lead review or investigation of the transaction.<sup>133</sup> The bill provides the Majority and Minority Leaders discretion to release these reports to other members of Congress where the transaction concerned implicates critical infrastructure in their home state.<sup>134</sup> The proposed bill also retains the four-year reporting requirement of the existing bill, but incorporates this as a subset of a new annual report.<sup>135</sup> Finally, where a proposed transaction concerns critical infrastructure, CFIUS must notify the governor of the affected state.<sup>136</sup>

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129. The proposed bill by its terms requires that country assessments be considered for all reviews and investigations, whether from a private citizen or government party. S. 3549 § 2(g).

130. *Id.* § 2 (h)(1).

131. *Id.* § 2 (j)(1) & (2) (providing requirements for notice and reports to Congress keyed to the stages of the review process set forth in subsections (a) and (b)).

132. *Id.* § 2(j)(3).

133. *Id.* § 2(j)(3)(C).

134. *Id.* § 2(j)(3)(D).

135. The annual report is required to include a discussion of the potential impact on the U.S. defense industrial base and critical infrastructure of foreign acquisitions during preceding year, and an aggregate analysis of the previous four years, prospective discussion of risks to national security and critical infrastructure, evaluation of whether there is credible evidence of a coordinated strategy by one or more countries or companies to acquire critical infrastructure or companies involved in research development or production critical technologies, and whether there are industrial espionage activities directed by foreign governments against private U.S. companies. *Id.* § 2(j)(4)(A)–(B); *see also* S. REP. NO. 109-264, *supra* note 109, at 13–15.

136. S. 3549 § 2(h)(2). The governor notice requirement stemmed from concerns voiced by state-level officials that they had no information regarding a pending transaction that could adversely affect their state, especially with respect to critical infrastruc-

The bill further disciplines the process by implementing safeguards for transactions that are notified to CFIUS. Withdrawal and resubmission of a filing triggers a mandatory forty-five day investigation.<sup>137</sup> The bill also requires CFIUS to monitor withdrawn transactions that nonetheless proceed and to initiate review if parties do not voluntarily re-file.<sup>138</sup> Where CFIUS resolves national security risks through mitigation agreements,<sup>139</sup> the bill provides for ongoing oversight of such agreements by CFIUS,<sup>140</sup> underwritten by a grant of authority to the Attorney General to investigate and enforce the agreements in the District of Columbia.<sup>141</sup>

The minimum threshold analysis introduced by the new bill shifts the existing balance by subordinating the open investment principle to national security concerns. This shift is reflected in the presumptions the bill creates regarding two categories of risks: those presented by ownership of infrastructures and technology deemed "critical" and those presented by the national origin of the proposed individual or country investment.<sup>142</sup>

The benefit of this shift is that in clearly articulating sources of risks, including long-term risks, the review process is more likely to ensure that questionable transactions are investigated by CFIUS, reducing the likelihood that risky transactions will "slip through the cracks." As noted above, the definition of critical infrastructure is broad and encompasses economic security criteria.<sup>143</sup> Consequently, the mandatory consideration

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ture, with view to discussing potential security concerns, subject to the same confidentiality requirements that apply to the federal government. S. REP. NO. 109-264, *supra* note 109, at 12.

137. S. 3549 § 2(b)(3).

138. *Id.* § 2(b)(4).

139. Though such mitigation agreements resolve most investigations in approval, the current review process does not address enforcement subsequent to approval. *See* S. REP. NO. 109-264, *supra* note 109, at 13.

140. S. 3549 § 2(i)(4).

141. Remedies include injunctive relief, damages, and divestiture. *Id.* § 2(i)(5).

142. The existing statutory framework was criticized in 2002 on similar grounds because the broad discretion conferred by the statute could be interpreted as broadly as the proposed bill. *See generally* Christopher R. Fenton, Note, *U.S. Policy Toward Foreign Direct Investment Post-September 11: Exon-Florio in the Age of Transnational Security*, 41 COLUM. J. TRANSNAT'L L. 195 (2002) (noting that the existing statutory framework in the new post-September 11 security context could be expanded to include consideration of threats identified on the basis of individual and organizational relationships, rather than investor nationality, as necessary to adequately address threats posed by non-state actors, and thus will expand scope of review to encompass foreign control of domestic industries, particularly those required for the anti-terror campaign).

143. "The term 'critical infrastructure' . . . includ[es] national economic security and national public health or safety . . . ." S. 3549 § 2(m)(2).

of critical infrastructure ensures that FDI that may entail long-term consequences for the United States through control of American assets, whereby foreign owners may exert their influence in a fashion inimical to American interests, for example by effectuating technology transfer or transferring American jobs overseas, is thoroughly investigated.<sup>144</sup>

In addition, requiring CFIUS to consider country assessments as part of its review ensures that each transaction is placed in a broader geopolitical context. With respect to the DPW deal, for example, the security risks presented by the UAE's acquisition of a controlling interest would be considered in light of factors like its proximity to Iran, the evidence that Pakistani scientist Abdul Qadeer Khan exploited Dubai's relaxed environment to smuggle nuclear components to Iran, Libya and North Korea, and its role as a conduit for funding of the September 11, 2001 terrorist attacks.<sup>145</sup> Furthermore, the inclusion of this factor in the review process creates an incentive for private parties to encourage states, and for states themselves, to establish a good track record of compliance with U.S. foreign policy.

Similarly, the expanded reporting requirements promise to introduce greater discipline in the process by ensuring Congress is informed about deals at initiation and conclusion, making oversight more effective.<sup>146</sup> A corollary benefit would be increased public and congressional confidence that reviews are handled as required by law, minimizing the public controversy that follows when a transaction is criticized in popular press. This, in turn, could prevent the public controversy that resulted in alienation of the investors in both the DPW and Smartmatic deals, and ultimately, divestment of their U.S. holdings.<sup>147</sup>

By the same token, this approach may be criticized as over-inclusive. The incorporation of mandatory consideration of transactions affecting critical infrastructure<sup>148</sup> includes a diverse array of industry sectors.<sup>149</sup> As

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144. See, e.g., GAO Mar. 1990, *supra* note 28, at 11, 25.

145. See S. REP. NO. 109-264, *supra* note 109, at 10–11.

146. *Id.* at 13.

147. See BBC NEWS, *Q&A*, *supra* note 60; NY TIMES, *Voting Machine Maker for Sale*, *supra* note 75.

148. 42 U.S.C. § 5195(c) (“[S]ystems and assets, whether physical or virtual, so vital to the United States that the incapacity or destruction of such systems and assets would have a debilitating impact on security, national economic security, national public health or safety, or any combination of those matters.”).

149. The *National Strategy for Homeland Security* identifies the critical infrastructure sectors as agriculture, food, water, public health, emergency services, government, defense industrial base, information and telecommunications, energy, transportation, banking and finance, chemical industry, postal, and shipping. NATIONAL STRATEGY, *supra* note 5, at 29–30. As the linchpin for all homeland defense legislation, see *id.* at 47–50.

discussed above, this creates a categorical presumption that investment in certain industries and physical assets presents a national security risk and introduces overt economic security factors that have been rejected in the past, in part because requiring consideration of transactions that were not at the core of national security would limit executive discretion to respond to national security considerations while also deterring foreign investment.<sup>150</sup> Worse, given the small membership of CFIUS, it risks defusing its focus and diverting limited resources from transactions CFIUS would otherwise prioritize.<sup>151</sup> This is especially true in light of the fact that critical infrastructure encompasses at least twenty-five percent of the economy.<sup>152</sup> Moreover, the incorporation of country assessments risks alienating foreign governments because they may be deployed as an overarching policy tool, whereby foreign investment is conditioned upon establishing a record of cooperation with U.S. policy goals.<sup>153</sup> Because “past CFIUS cases indicate it is inherently more difficult for a CFIUS agency to argue that foreign firms from allied countries

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*See generally* MOTEFF & PARFOMAK, *supra* note 123 (helpful overview of evolution of the definition of critical infrastructure).

150. *See* Holmer et al., *supra* note 105, 608, 615–17 (listing series of bills introduced in the early 1990s that attempted to introduce economic security criteria but failed); LARSON & MARCHICK, *FOREIGN INVESTMENT*, *supra* note 7, at 28; Deborah M. Mostaghel, *Dubai Ports World Under Exon-Florio: A Threat To National Security or a Tempest In a Seaport?*, 70 ALB. L. REV. 583, 591–3, 622 (2007).

151. Byrne, *supra* note 108, at 905 (noting that inclusion of economic security in CFIUS review would dilute the focus from “true threats” and allow its diversion to general economic protectionism with the added risk that foreign nations would emulate this policy, jeopardizing U.S. foreign investments abroad).

152. LARSON & MARCHICK, *FOREIGN INVESTMENT*, *supra* note 7, at 29.

153. *See* Wysocki, Jr. et al., *supra* note 14. Unlike the Senate bill, the U.S. Model Bilateral Investment Treaty rejects nationality as a proxy for any purpose. Article 9(1) states “[n]either Party may require that an enterprise of that Party that is a covered investment appoint to senior management positions natural persons of any particular nationality.” Article 9(2) allows a party to require a majority of a managing board of directors “be of a particular nationality or resident in a particular territory, provided that the requirement does not materially impair the ability of the investor to exercise control over its investment.” U.S. Department of State, U.S. Model Bilateral Investment Treaty (2004), <http://www.state.gov/documents/organization/38710.pdf>. One scholar has suggested that the proliferation of bilateral investment treaties, despite the failure of the international community in the aggregate to attain consensus on general principles governing foreign investment, is evidence of legal obligations undertaken by states has resulted in “something like customary law.” Andreas F. Lowenfeld, *Investment Agreements and International Law*, 42 COLUM. J. TRANSNAT'L L. 123, 150 (2003).

may threaten national security” this is particularly problematic as a criteria for FDI risk assessment.<sup>154</sup>

In expanding CFIUS’ scope through inclusion of critical infrastructure and country assessments as factors, the bill broadens the sweep of CFIUS review and investigation, effectively expanding its operational definition of “national security” but without articulating any clear guidance to investors.<sup>155</sup> In this way, the bill unnecessarily risks alienating foreign investors and governments because differing views of national security are already accounted for in CFIUS membership.<sup>156</sup> By decreasing CFIUS’ discretion and increasing the number of factors for consideration, the bill implicates an underlying concern that the operational definition of national security currently employed by CFIUS is too narrow.<sup>157</sup> Broadly defined, “national security” may encompass concerns about the growth and direction of the U.S. economy at large, consequences for the U.S. economy where foreign capital may be from a country vulnerable to social or political crises and general commercial competitiveness from risks presented by technology transfer.<sup>158</sup> Since different views of national security are currently taken into account in the diverse CFIUS membership,<sup>159</sup> where such views are materially different, their consid-

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154. GAO Feb. 1991, *supra* note 95, at 8. This trend is also reflected in the larger pattern of foreign investment discussed above, which noted that the predominant source of FDI in the United States is countries typically allied with the United States. Alienating investments from countries that are less clearly allied runs counter to the principle of open investment whereby aligning economic interests contributes to overall stability, and consequently to the maintenance of national security. *See* discussion *supra* Part II.

155. An article discussing the 1991 regulations promulgated by the Treasury Department noted that the regulations failed to define national security with any specificity, despite complaints from investors and multi-national corporations that had lobbied for a bright line test because the regulations provided inadequate guidance. *See* Holmer et al., *supra* note 105, at 595, 608–10.

156. The debate regarding the definition of “national security” in Exon-Florio has plagued the review process since its inception. *See id.* In 1990, a GAO report concluded that “the absence of a specific definition of national security” had not negatively impacted CFIUS investigations. GAO Mar. 1990, *supra* note 28, at 11. In 2003, CFIUS was expanded to include the DHS, which conducts reviews of critical infrastructure to identify and handle threats. *See* Exec. Order No. 13,286, 68 F.R. 10,619 (Feb. 28, 2003).

157. At present, the term “national security” is undefined. In practice, the scope of the review process provides an operational definition. A narrow definition concerns primarily firms whose business derives from defense contracts. A broader definition encompasses firms engaged in non-defense commercial business. *See* GAO Mar. 1990, *supra* note 28, at 11.

158. *See, e.g.,* GAO May 1990, *supra* note 11, at 3.

159. By requiring CFIUS to examine security risks in terms of aggregate effects over long-term, and thus limiting foreign investment could “translate into inferiority in the development, prototyping, manufacturing and production and product improvement

eration is ensured by the CFIUS practice of proceeding by consensus.<sup>160</sup> This means the dissenting vote of any one member automatically triggers the second-stage review, whereupon the dissenting vote must be brought to the attention of the President as part of the final determination whether to exercise his or her authority to block a deal.<sup>161</sup>

In addition to expanding the operative definition of national security, the bill also expands reporting requirements, but fails to provide clear guidelines for confidentiality and disclosure on the part of Congress, risking politicization of a review process that had previously been safely sequestered from Congress.<sup>162</sup> This in turn, combined with the requirement to notify and consult with state governors regarding investment in their state's critical infrastructure,<sup>163</sup> which by definition includes economic security criteria, introduces a strong likelihood that the review process will be exploited for protectionist ends.<sup>164</sup>

Finally, the combination of increased oversight and stricter enforcement of national security mitigation agreements could entail inappropriate involvement in the business decisions of companies.<sup>165</sup> Especially in conjunction with other aspects of the bill, the provisions governing mitigation agreements introduce a risk of protectionism, whereby CFIUS could become a vehicle for the imposition of performance requirements on foreign acquisitions by U.S. companies.<sup>166</sup> Because these mitigation agreements have the full force of law and are subject to investigation and enforcement, the bill may be a further deterrent to foreign investors faced with internalizing the cost of broad U.S. policy concerns regarding national security.<sup>167</sup>

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strategies . . . ." Bobrow & Kudrle, *supra* note 11, at 74-5; *see also* Nowak, *supra* note 10.

160. Byrne, *supra* note 108, at 909.

161. *Id.*

162. *See* LARSON & MARCHICK, FOREIGN INVESTMENT, *supra* note 7, at 15-17.

163. S. 3549 § 2(h)(2).

164. *See* LARSON & MARCHICK, FOREIGN INVESTMENT, *supra* note 7, at 29. The existing review process has itself been criticized as a vehicle for domestic protectionism. *See generally* Shearer, *supra* note 42. The litigation brought by the Port Authority of New York and New Jersey and the Miami-based stevedoring company cited contractual claims and concerns over security in their suits to block the deal. Concerns regarding layoffs, etc. may have been an underlying motivation for the suit. *See, e.g.,* WALL ST. J. ONLINE, *Ports Deal News Tracker*, *supra* note 53.

165. GAO Sept. 2002, *supra* note 102, at 24, 27.

166. *Id.* at 28.

167. A corporation's primary duty is to its shareholders; placing the burden of mitigating security issues with respect to critical infrastructure that encompasses bridges and flu vaccinations places too much burden on private capital. *See* J. Michael Littlejohn, *Using all the Kings Horses for Homeland Security: Implementing the Defense Production Act*

*C. Does the Senate Bill Enhance National Security?*

On balance, the new bill shifts the existing paradigm, at minimum, by bringing the national security principle on par with, if not elevating it over, the open investment principle. In contrast, in the existing paradigm, the national security principle is often subordinate to the open investment principle, while allowing discretion as needed. This paradigm shift finds symbolic and substantive manifestation in the appointment of the Secretary of Defense as the Vice-Chair for CFIUS.<sup>168</sup> Because the bill risks that American businesses may have greater difficulty courting foreign investors, with the consequence that over time, flows of FDI could be reduced, the question becomes whether the Senate bill accomplishes this result with appreciable benefits for national security. The application of the two different paradigms to the DPW and Smartmatic deals helps illustrate the different schema in action.

With respect to the DPW transaction, the principle concerns were that CFIUS failed to subject the transaction to the second-stage forty-five day review required by existing law, and that even if it had, CFIUS failed to properly consider the larger geo-political context of the deal, especially as related to national security risks to ports within the United States.<sup>169</sup> Under the new paradigm, the corporate entity owned by the UAE would be required to notify CFIUS of the deal, and under the expanded reporting requirements, Congress would also be notified, allowing it to ensure that the second-stage forty-five day investigation was conducted as required by both the new bill and existing law.<sup>170</sup> However, the mitigation agreement negotiations that occurred during the first-stage review of the DPW acquisition would probably not have been materially different, although the negotiations may have been accomplished without the furor that surrounded the transaction and perhaps avoiding the related public pressure that eventually scuttled the U.S. portions of the deal.<sup>171</sup>

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*for Disaster Relief and Critical Infrastructure Protection*, 36 PUB. CONT. L.J. 1, 2 (2006) (observing the important role of the private sector, the negative publicity where risks to infrastructure are identified, how this may operate as a disincentive to effective collaboration with the private sector, and identifying the legal framework for government authority to compel cooperation from the private sector in the event of natural disaster or terrorist attack).

168. S. 3549 § 2(c)(3); Byrne, *supra* note 108, 909 (arguing that maintaining the Department of Treasury as chair ensures primacy of open investment policy while allowing agencies with different mandates adequate authority to ensure that national security concerns are addressed; changing the chairmanship risks upsetting this balance without real national security benefit).

169. See Hufbauer, *supra* note 52; Kaplan, *UAE Purchase*, *supra* note 3.

170. S. 3549 § 2(j)(1)–(2).

171. BBC NEWS, *supra* note 60.



It is unclear how CFIUS' consideration of the mandatory country assessments in evaluating the risks presented by the transaction would affect the review; it is possible that the UAE's track record as a conduit for arms and money to terrorists and rogue states would force CFIUS to recommend blocking the deal at the conclusion of the second-stage investigation.<sup>172</sup> Because it is unlikely that the national security mitigation agreements would have been materially different, it is not clear that any appreciable security benefit would be attained by the more disciplined minimum threshold paradigm reflected in the bill. At minimum, the issue would be brought to the President, including any dissenting views, and on the facts of this case, the deal would probably have been allowed to proceed.<sup>173</sup> In this case, as the President noted defending his approval of the transaction,<sup>174</sup> the factual misconception that was the kernel of the controversy is two-fold: the nature of the property interest in the ports (here merely leases), and the security responsibilities entailed by that interest.<sup>175</sup> For example, it is common place in the United States for foreign corporations to own and operate U.S. ports.<sup>176</sup> Port security remains a primary responsibility of the U.S. Coast Guard, and the U.S. Customs and Border Protection supervises security for cargo, and U.S. citizens staff most ports.<sup>177</sup> Consequently, risks relating to ports as a conduit for foreign personnel and cargo, including terrorists or bombs, remain under the purview of the U.S. government irrespective of who manages vessels and ports.<sup>178</sup> Thus, the security risks specifically implicated by the transaction were likely mitigated by the agreement, and those that were not were well beyond the power of DPW to mitigate.<sup>179</sup> The principle concerns raised by critics were symptomatic of larger concerns regarding U.S. vulnerability in ports at large and not specific to DPW. Regardless

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172. S. 3549 § 2 (c)(7) (mandatory country assessments).

173. 31 C.F.R. § 800.504 (regulation requiring presentation of dissenting views to President).

174. Major Garrett et al., *Bush Says He Will Veto Any Bill to Stop UAE Port Deal*, FOX NEWS, Feb. 22, 2006, <http://www.foxnews.com/story/0,2933,185479,00.html> (describing Bush Administration's defense of President's approval of the DPW transaction).

175. JOHN FRITTELLI, *TERMINAL OPERATORS AND THEIR ROLE IN U.S. PORT AND MARITIME SECURITY*, CRS RL33383 (Apr. 20, 2006) (providing a comprehensive overview of the operation and security of U.S. ports).

176. State-owned Singaporean shipping company, Neptune Orient Lines, operates U.S. ports. Kaplan, *UAE Purchase*, *supra* note 3.

177. *See generally* FRITTELLI, *supra* note 175; *see also* Kaplan, *UAE Purchase*, *supra* note 3.

178. Kaplan, *UAE Purchase*, *supra* note 3.

179. Bilkey, *Testimony*, *supra* note 56, 59 and accompanying text (itemizing concessions, including, of specific relevance here, the provision of personnel files to DHS).

of the outcome of this particular transaction, the security vulnerability of U.S. ports remains.<sup>180</sup>

The consequences for the Smartmatic deal are slightly different. The Smartmatic deal concerned the acquisition of a relatively small, privately held concern, Sequoia Voting Systems, based in Oakland, California, which, as discussed, never underwent CFIUS review.<sup>181</sup> The principle concern with the Smartmatic deal was that the transaction implicated the government of Venezuela and that electronic voting systems are too central to U.S. national interests and too vulnerable to tampering.<sup>182</sup> Whether the new minimum threshold paradigm proposed by the Senate would be more likely to bring the Smartmatic deal under review by CFIUS depends on a few different factors. If the Venezuelan government had an interest in the transaction, either itself or a person acting on its behalf, the parties to the deal would be required to file with CFIUS (under both paradigms).<sup>183</sup> However, because the deal involved neither the government of Venezuela, nor a person acting on behalf of Venezuela, it is not clear that this acquisition would have been brought to the attention of CFIUS.<sup>184</sup> Two principle possibilities remain. Given the expansive definition of critical infrastructure, whether the transaction would be submitted for review under the new paradigm depends on whether voting systems would be considered critical infrastructure.<sup>185</sup> The second possibility under the new paradigm is if the Secretary of Defense determined Venezuela constituted a regional threat.<sup>186</sup> If the deal were notified to CFIUS through either mechanism, under the new paradigm, Congress would have been alerted to the occurrence of the transaction.

In contrast, under the existing paradigm, CFIUS would neither be required to nor precluded from consideration of this transaction. In addition, under the existing law, if the transaction were notified to CFIUS, both the Department of Defense or the DHS (both currently represented on CFIUS) could review the transaction and conclude that foreign ownership of a voting systems manufacturer constituted a potential impairment of national security. In this case, any security concerns could be addressed through mitigation agreements, without the need to subject the

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180. As reflected in the enactment of broad port security legislation following the DPW controversy. See discussion *infra* notes 208–209 and accompanying text.

181. See discussion, *supra* Part III.B.

182. See SVS Oct. 29, 2006 Press Release, *supra* note 73; GAO Elections, 2007, *supra* note 78.

183. S. 3549 § 2(b)(5) (mandatory notice requirements for foreign governments); see *supra* note 93.

184. See Golden, *supra* note 1.

185. S. 3549 § 2(g)(1).

186. *Id.* § 2(g)(6)(B).

transaction to the enhanced scrutiny required by the additional factors in the Senate bill. Under both the existing law and the proposed law, the larger policy concern regarding the vulnerability of electronic voting systems, like the larger problem with ports following the scuttled DPW deal, remains.

Thus, the new paradigm may have some impact in increasing the number of investigations notified to CFIUS for review, but without appreciably enhancing national security, and potentially at significant long-term cost.

#### V. RESOLVING THE EXON-FLORIO PROBLEM

As illustrated above, the existing paradigm strikes a preferable balance between open investment and national security, and preserves the substance of the principle underlying open investment, which maintains that aligning economic interests in the long term provides greater stability, and ultimately, security.<sup>187</sup> Despite its preferable balance of open investment and national security values, the analysis above reveals several critical and interrelated problems in the current review and investigation process: 1) CFIUS does not necessarily follow the review process mandated by law;<sup>188</sup> 2) CFIUS failure to keep Congress abreast of its review process may create a volatile mix of congressional and public lack of confidence that results in divestment despite lack of any credible evidence of a threat to national security;<sup>189</sup> and 3) CFIUS failure to inform Congress may also result in an inappropriate focus on security risks created by a specific transaction, diverting focus from the larger security issue of which the transaction is but a part.<sup>190</sup>

While the proposed bill seeks to address these concerns, it does so at great cost by creating categorical presumptions as to who and what present national security concerns at risk of alienating foreign investments and governments, which could redound to the detriment of the American economy in the long run.<sup>191</sup> Deterring investment in U.S. companies means capital will flow elsewhere and alienates private and government parties with whom the United States would gain the most by cooperat-

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187. See Kaplan, *Foreign Ownership*, *supra* note 11.

188. See Mostaghel, *supra* note 150, at 620 (CFIUS failed to conduct the forty-five day investigation of the DPW transaction as required by the existing law).

189. See *id.* at 622 (describing the partisan melee on Capital Hill over the DPW deal).

190. See Byrne, *supra* note 108, at 902–05.

191. “There are those who would broaden Exon-Florio to include threats to national objectives such as industrial competitiveness, but that sort of inclusiveness would basically cover exactly those nations with whom technological cooperation has the most to offer for U.S. objectives.” Bobrow & Kudrle, *supra* note 11, at 90.

ing.<sup>192</sup> On the other hand, failing to address the problems implicated by lack of congressional and public confidence in the CFIUS review process may implicate similar long-term costs by subjecting specific transactions to unwarranted and partisan scrutiny.<sup>193</sup>

Alienation of private sector and government foreign interests presents very real costs.<sup>194</sup> For example, concessions regarding access to employment records in the final stages of the DPW deal represents a missed opportunity to obtain inside information about global shipping, and as a result, for law enforcement and intelligence agencies to gain insight into global smuggling of terrorists and weapons.<sup>195</sup> Furthermore, encouraging the deal would have helped ensure DPW instituted practices compliant with U.S. security standards in U.S. ports as well as abroad, notably the port in Dubai.<sup>196</sup> Similarly, enlisting the cooperation of Smartmatic in developing electronic voting systems standards and in ensuring that Smartmatic units meet these standard would likely result in the diffusion of these standards to elections in Venezuela, if for no other reason than economies of scale.<sup>197</sup>

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192. Nowak, *supra* note 10, at 1030–31.

193. In the controversy following the DPW deal, it was observed that congressional case-by-case review of commercial transactions at large would generate untenable uncertainties and potential delays for foreign investors with a chilling effect, but this is equally true whether the scrutiny is de jure or de facto. See C. Fred Bergsten, Op-Ed., *Avoiding Another Dubai*, WASH. POST, Feb. 28, 2006, available at <http://www.iie.com/publications/opeds/oped.cfm?ResearchID=603>; see also *Bush Threatens Veto in Ports Row*, BBC NEWS, Feb. 22, 2006, <http://news.bb.co.uk/go/pr/fr/-/2/hi/americas/4737940.stm>.

194. The private sector and foreign governments are identified as critical partners in the *National Strategy for Homeland Security*. See NATIONAL STRATEGY, *supra* note 5, at 33–35.

195. Block, *supra* note 56.

196. DPW, with the \$6.8 billion purchase of P&O, became the third largest port operator in the world. Kaplan, *UAE Purchase*, *supra* note 3; see also LARSON & MARCHICK, FOREIGN INVESTMENT, *supra* note 7, at 20; King, Jr., *supra* note 59. The significance of DPW's willingness to assume responsibility for purchasing, deploying and maintaining radiation detection systems cannot be underestimated. At this stage, although there are serious questions as to the efficacy and value of next-generation systems, DHS figures estimate an increase of over \$320,000 per unit to up-grade existing security, a process that would not be complete at all U.S. ports until 2013. A recent report indicated these costs could be well below actual cost. GAO, COMBATING NUCLEAR SMUGGLING: DHS'S DECISION TO PROCURE AND DEPLOY THE NEXT GENERATION OF RADIATION DETECTION EQUIPMENT IS NOT SUPPORTED BY ITS COST-BENEFIT ANALYSIS, GAO-07-581T, Mar. 14, 2007 (Testimony of Gene Aloise).

197. For example, the results of the widely criticized 2004 election in Venezuela were eventually audited. The Carter Center participated in the audit and attested that the Smartmatic voting machines operated "flawlessly." Juan Forero, *Opposition Rejects Au-*

Alienating the government of UAE would have further concrete costs. The Dubai government runs the Middle East's biggest airline, Emirates Air, just one of a several UAE government-owned companies with substantial investments worldwide, including in the United States.<sup>198</sup> Despite its mixed record supporting U.S. foreign policy, the UAE gave \$100 million to assist victims of Hurricane Katrina.<sup>199</sup> In addition, in a "symbol that the United States trusted the UAE and took the UAE seriously," the UAE government was permitted to purchase 80 F-16 fighter jets in a \$6.4 billion deal in 2000.<sup>200</sup> Following criticism that funds funneled through its hub financed the terrorist attacks of September 11, 2001, the UAE bolstered its anti-money laundering and terror-financing laws and generally increased oversight.<sup>201</sup> The UAE was also the first country to implement the U.S. Cargo Security initiative to pre-screen containers at foreign ports and hosts five U.S. Customs Officials.<sup>202</sup> Finally, the Jebel Ali Port is an important global host to the U.S. Navy, more so than any other foreign port.<sup>203</sup> The DPW acquisition was part of the UAE's overall plan to develop a stable, international financial center based in Dubai, transforming oil wealth into longer term investments, diversifying the economy and increasing the region's integration into the global economy.<sup>204</sup>

Instead of burdening the influx of much-needed foreign capital with broad-based U.S. security concerns, the central problems of the Smartmatic and DPW deals should be addressed. Namely, reform should seek to increase congressional confidence that a thorough review has been conducted,<sup>205</sup> while providing a mechanism to identify and address larger security vulnerabilities that may be exposed in the CFIUS review process. As the GAO noted, "[t]hese questions need to be addressed at a higher policy-making level and in a broader context than the case-by-

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*dit Plan in Venezuela Recall Vote Dispute*, N.Y. TIMES, Aug. 19, 2004, at A5. On the emerging controversy, see Juan Forero & John Schwartz, *Venezuelan Recall Is In Dispute Even Before the Vote*, N.Y. TIMES, June 11, 2004, at A3; Brian Ellsworth, *A Crucial Vote for Venezuela and a Company*, N.Y. TIMES, July 20, 2004, at W1.

198. Spindle et al., *supra* note 3 (these companies purchased major historic hotels and landmarks in New York, San Francisco, and London).

199. Joel Brinkley and Craig S. Smith, *Storm and Crisis: Foreign Aid; Offers Pour In, But the U.S. Is Unprepared*, N.Y. TIMES, Sept. 8, 2005, at A25.

200. Spindle et al., *supra* note 3.

201. *Id.*

202. *Id.*

203. *Id.*

204. Spindle & El-Rashidi, *supra* note 27.

205. See LARSON & MARCHICK, FOREIGN INVESTMENT, *supra* note 7, at 25–26.

case approach presently afforded by CFIUS.”<sup>206</sup> What is striking about the DPW and Smartmatic controversies is that while both represented lost opportunities for the United States to collaborate with the private sector to implement national security policy on a global scale,<sup>207</sup> one positive parallel development was the drafting of legislation to address the larger security concerns implicated in the transactions. In 2006, Congress enacted laws to address the unique security concerns raised in ports.<sup>208</sup> In the following year, bills were introduced to Congress to secure electronic voting systems, but as of the time of publication, none has yet passed.<sup>209</sup> The costs of these security concerns should not be assessed on each individual transaction, but by legislation to address the larger vulnerability that may emerge from the inquiry. The value of congressional oversight in this context is not only to ensure that CFIUS appropriately implements presidential authority to review transactions,<sup>210</sup> but more importantly to provide oversight on the second prong of the Exon-Florio test: where existing laws provide the President insufficient authority to protect national security.<sup>211</sup> As illustrated by the Smartmatic and DPW deals, the goal of congressional oversight should be to focus attention on specific security vulnerabilities that may not be adequately addressed through mitigation agreements in recognition of the fact that the identifiable risks that emerge from a particular transaction are in many cases only a small part of a given vulnerability.

To the extent that greater congressional oversight is required or desirable, it should be strictly circumscribed to avoid the partisan melee that ultimately alienated the investors in the DPW and Smartmatic deals. As one author notes, although “Congress has a role in forming U.S. foreign and national security policy, . . . its role is more appropriately a secondary one of oversight and review.”<sup>212</sup> While the proposed bill purports to

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206. GAO Feb. 1991, *supra* note 95, at 10.

207. See Stephen Flynn & Daniel B. Prieto, Op-Ed., *Capitalizing on the Private Sector to Protect the Homeland*, WASH. POST, Apr. 28, 2006.

208. Security and Accountability For Every Port Act of 2006, Pub. L. No. 109-347 (codified in scattered sections of 9 U.S.C and 46 U.S.C.).

209. Vote Integrity and Verification Act of 2007, S. 559, 110th Cong. (2007); Voter Confidence and Increased Accessibility Act of 2007, H.R. 811, 110th Cong. (2007).

210. Cf. Mostaghel, *supra* note 150, at 620–22 (rejecting any change to the existing law and suggesting CFIUS do a better job following it).

211. See 50 U.S.C. app. § 2170(e).

212. Russell J. Bruemmer, *Intelligence Community Reorganization: Declining the Invitation to Struggle*, 101 YALE L.J. 867, 880 (1992). As Bruemmer notes, where national security and foreign relations are concerned, the executive powers are at their constitutional apex. In fact, the executive branch will have the best and most accurate information both about the geo-political context of a particular transaction and the degree to

maintain confidentiality, its notice and reporting mechanisms are sure to embroil transactions in partisan domestic politics, introducing a substantial risk to the transactions concerned.<sup>213</sup> Furthermore, the bill provides no specific measures for ensuring confidentiality, while injecting sensitive national security information and proprietary corporate information into the partisan and political arena of Congress.<sup>214</sup>

At most, the annual reports proposed in the new bill should permit sufficient oversight to ensure that Congress is confident CFIUS conducts a thorough review and to alert Congress to the larger security issues that emerge out of a particular transaction; any expanded notice and reporting requirements should be rejected.<sup>215</sup> In the event that further scrutiny demonstrates a need for enhanced oversight, a committee modeled after the Senate's Select Committee on Intelligence provide may a viable solution.<sup>216</sup>

The Select Committee emerged relatively recently, in 1976, at around the same time a committee to review FDI was first considered.<sup>217</sup> The interests at stake are similar; the oversight responsibilities implicate national security and core executive branch activity, with a strong need for confidentiality. To implement its oversight responsibilities, the Senate created an oversight committee with limited membership, strict voting procedures and rules governing confidentiality of information, and imposed consequences for failure to comply. More specifically, membership in the Senate Select Committee on Intelligence is cooperative through appointment by the President based on recommendations of the Senate leadership; membership must represent members from both political parties.<sup>218</sup> Any disclosure of confidential information by the Committee requires first, that the Committee vote, and if a majority agrees that disclosure is in the public interest, the Committee must notify the President, who may object that the threat to the national interest posed by such disclosure outweighs the public interest in that confidential information, whereupon the Committee may vote to refer to the question of

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which it presents a threat to national security; the President is also the party on whom failure will be most prominently visited. *Id.* at 878–80 (analyzing the roles of the executive and legislative branches with respect to intelligence community reform).

213. The mandatory notification to state governors, S. 3549 § 2(h)(2), and case-by-case notice to Congress, *id.* § 2(j).

214. See *id.* § 2(h)(1) (information filed with CFIUS shall be exempt from disclosure, but instituting no mechanisms or penalties).

215. LARSON & MARCHICK, FOREIGN INVESTMENT, *supra* note 7, at 29.

216. On reporting requirements introduced in the new bill, see *id.* § 2(j).

217. S. Res. 400, 94th Cong. (1976) (establishing the Senate Select Committee on Intelligence); see also Breummer, *supra* note 212, at 873–4.

218. S. Res. 400, 94th Cong. app. A, § 2(a)(1) & (a)(2) (1976).

disclosure of such information to the Senate at large in closed session.<sup>219</sup> Aside from this procedure for disclosure, all other information is confidential, and any individual that discloses information in violation of these procedures may be subject to censure, including removal from office.<sup>220</sup> In so doing, the regulations address the need for oversight while remaining cognizant of the importance of confidentiality and the vulnerability of congressional oversight to inappropriate politicization. As applied to CFIUS, a similar model would provide specific measures to ensure that congressional oversight is employed only to ensure the law is followed and where executive review reveals inadequacy in presidential authority to address national security exigencies. Limiting the purview of oversight in this way, combined with the introduction of strict procedural requirements to ensure that any such committee is bipartisan and the enforcement of confidentiality with concrete penalties limits the risk of politicization of particular transactions and the disclosure of confidential information (whether related to national security or to the interests of the parties to the transaction), while achieving the objective of oversight: that Congress receives timely notice of larger security risks where the President's authority is inadequate. This, in turn, would ensure the primacy of traditional principles of U.S. open investment policy.

## VI. CONCLUSION

The DPW deal precipitated a controversy that resulted in renewed scrutiny of the role of FDI in the United States. The legislative reform of the CFIUS review process proposed in the wake of this controversy represents a dramatic shift in traditionally open U.S. investment policy. In particular, the minimum threshold paradigm for FDI review introduced by the new bill limits CFIUS discretion with respect to the interpretation of who and what represent national security risks, without tangible security benefit. At the same time, the new bill sends a hostile message, a shot across the bow, to foreign investors. The DPW and Smartmatic transactions and their subsequent divestiture represent a paradigmatic failure to advance U.S. strategic interests on a global scale through partnership with corporations operating worldwide. Furthermore, the proposed bill risks that individual transactions will be burdened with broader national security concerns. To maintain the primacy of U.S. open investment policy, it may be necessary to expand congressional oversight to restore congressional and public confidence in the post-September 11 era of heightened security concern. To the extent such oversight is neces-

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219. *Id.* § 8(a) & (b).

220. *Id.* § 8(c)–(e).



sary, it should be strictly circumscribed. In this context, oversight is required to ensure that CFIUS applies the existing law appropriately and to ensure Congress may respond with legislation specific to any larger security vulnerability revealed in the review process. Furthermore, any expansion of congressional review should include confidentiality requirements enforced by strict procedures and penalties that resemble the procedures of the Senate Select Committee on Intelligence.

## VII. EPILOGUE

As this Note was prepared for publication, the Foreign Investment and National Security Act of 2007 was signed into law by President Bush.<sup>221</sup> While a complete review of the new law is beyond the scope of the Note at this late date, some preliminary observations are in order.

The new law reflects many of the characteristics of the minimum threshold paradigm proposed in the bill analyzed in this Note. In particular, the new law changes CFIUS membership, expands CFIUS' scope of review while reducing its discretion, and substantially increases congressional oversight.

Under the new law, the most notable new CFIUS members are the Secretary of Labor and the Director of National Intelligence.<sup>222</sup> In addition, unlike the bill analyzed above, which threatened to subordinate the open investment principle to that of national security by designating the Secretary of Defense as Vice Chairperson of CFIUS,<sup>223</sup> the new law retains the Secretary of the Treasury as the sole chairperson of CFIUS.<sup>224</sup> The addition of the Secretary of Labor remains troubling, however, in that it may signal a shift from a narrow national security focus to one that may also entail broader national security concerns like the preservation of domestic jobs.<sup>225</sup>

As in the minimum threshold paradigm analyzed above, the new law creates a presumption that foreign control of critical infrastructure creates a national security risk.<sup>226</sup> In the new law, when an investment by a foreign entity could result in control of critical infrastructure and any security risks remain unmitigated, a second-stage, forty-five day investi-

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221. Foreign Investment and National Security Act of 2007, PL 110-49 (HR 556), 121 Stat. 246 (2007) (to be codified in 50 U.S.C. app § 2170). The new law establishes CFIUS, which was formed by delegation of authority via executive order, by statute. *Id.* § 3(k)(1).

222. Both are nonvoting, ex officio members. *Id.* § 3(k)(2)(H) & (k)(2)(I).

223. See *supra* note 168 and accompanying text.

224. *Id.* § 3(k)(3).

225. *Id.* § 3(k)(2)(H).

226. See discussion *supra* Part IV.B.

gation is required.<sup>227</sup> In addition, critical infrastructure is incorporated into the law's definition of national security and into the list of factors for consideration by CFIUS, expanding the scope of CFIUS review at least as much as the minimum threshold paradigm.<sup>228</sup> In marked contrast to the minimum threshold paradigm, however, the potentially unlimited sweep of this expansion is ameliorated by the requirement that the Secretary of the Treasury shall publish "guidance on the types of transactions that the Committee has reviewed and that have presented national security considerations . . . ."<sup>229</sup>

The new law also expands the scope of CFIUS review to include evaluation of the country of origin's track record of compliance with non-proliferation regimes and its "relationship" with the United States.<sup>230</sup> These factors are the same factors that the bill analyzed in the body of this Note characterized as "Assessments of Foreign Countries."<sup>231</sup> The new law limits consideration of these additional factors for review to those investments by or on behalf of a foreign government.<sup>232</sup> Thus, on its face and in contrast to the minimum threshold paradigm discussed above, this expansion of CFIUS' scope of review does not by its terms require CFIUS to consider this evidence when evaluating the security risk posed by a non-government affiliated private foreign investor.<sup>233</sup> On the other hand, the new law requires any mitigation agreement be "based on a risk-based analysis, conducted by the Committee, of the threat to national security of the covered transaction."<sup>234</sup> "Risk-based analysis" is not a defined term; however, the new law's definition of national security incorporates "issues relating to 'homeland security.'"<sup>235</sup> The combination of these elements in the new law, like in the minimum threshold paradigm analyzed in the body of this Note, present a risk that individual

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227. 121 Stat. 246 § 2 (b)(2)(B)(i)(III). On the timing requirements for investigations, see *id.* § 2 (b)(2)(C).

228. "The term 'national security' shall be construed so as to include those issues relating to 'homeland security', including its application to critical infrastructure." *Id.* § 2(a)(5). Critical infrastructure is also incorporated into the factors for CFIUS consideration. *Id.* § 4 (f)(4). The inclusion of a definition of "national security" for the purposes of CFIUS review is itself a significant change. See *supra* note 120.

229. 121 Stat. 246 § 2 (b)(2)(E).

230. *Id.* § 4(4).

231. See discussion *supra* Part IV.B.

232. In the chapeau to the subsection, 121 Stat. 246 § 4(4), the new law states "as appropriate, and particularly with respect to transactions requiring an investigation under subsection (b)(1)(B)," i.e. those instances where CFIUS "determines that the covered transaction is a foreign government-controlled transaction . . . ." *Id.* § 2(b)(1)(B).

233. See discussion *supra* Part IV.B.

234. 121 Stat. 246 § 5(l)(1)(B).

235. *Id.* § 2(a)(5)

transactions, whether they involve government or private foreign investors, may be required to internalize the costs of broad homeland security issues in order to secure CFIUS approval.<sup>236</sup>

The lack of tracking for drop-outs from the review process and lack of enforcement authority for mitigation agreements noted as problems in the law prior to amendment<sup>237</sup> have also been addressed in the new law.<sup>238</sup> While these were addressed in the unadopted bill analyzed above, the new law strikes a better balance by allowing CFIUS to promulgate its own methods for evaluating compliance and by ensuring that compliance with any mitigation agreements will not place “unnecessary burdens on a party to a covered transaction.”<sup>239</sup>

Finally, like the minimum threshold paradigm, the new law expands congressional oversight of CFIUS’ reviews and investigations.<sup>240</sup> The new law requires case-by-case notice to Congress.<sup>241</sup> However, unlike the minimum threshold paradigm, the new law does not require notice at the initiation of reviews and investigation, and instead, limits these notices to certifications at the completion of the first-stage review and second-stage investigation.<sup>242</sup> In addition, unlike the minimum threshold paradigm, the new law does not require CFIUS to notify the governor when a transaction involves critical infrastructure in that governor’s state.<sup>243</sup> The new law, like the bill analyzed above, also modifies the current law’s quadrennial report requirement to include an annual report.<sup>244</sup> By limiting notices to Congress to the concluding stage of the review and investigation and by removing the requirement to notify state governors, the new law strikes a better balance than the bill analyzed above by achieving increased public and congressional confidence in the thoroughness of review while limiting the potential for the damaging consequences of unnecessary publicity and politicization.<sup>245</sup>

In conclusion, the new law bears a striking resemblance to the minimum threshold paradigm introduced by the bill analyzed in the body of this Note. The new law contains some important differences however, and as a consequence, it strikes a better balance between national security and the principle of open investment. In particular, the provisions

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236. See discussion *supra* Part V.

237. See discussion *supra* Part IV.B.

238. 121 Stat. 246 § 5(l)(1)–(3).

239. *Id.* § 5(l)(3)(B)(ii) & (l)(3)(B)(ii)(II).

240. *Id.* § 2(b)(3) (certifications to Congress) & § 7 (increased oversight by Congress).

241. *Id.* § 2(b)(3).

242. *Id.*

243. See discussion *supra* Part IV.C.

244. 121 Stat. 246 § 7(b).

245. See discussion *supra* Part IV.B.

that require the Secretary of the Treasury to provide guidance to investors regarding which transactions typically raise national security considerations may allay the concerns of many foreign investors. On the other hand, the incorporation of homeland defense issues and critical infrastructure into the definition of national security risks burdening individual transactions with the costs of larger U.S. security vulnerability that should be addressed through national security legislation like the ports security act discussed above. Whether the increased oversight by Congress provided in the new law will be sufficient to restore public and congressional confidence while adequately circumscribing congressional involvement so as to avoid a repeat performance of the damaging controversies that resulted in the unnecessary divestment of U.S. interests in both the DPW and Smartmatic transactions remains to be seen.

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